UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF PUERTO RICO

RUBEN GARCIA, derivatively for the benefit of and on behalf of the Nominal Defendant POPULAR INC., Plaintiff, vs. RICHARD L. CARRIÓN, DAVID H. CHAFEY, JORGE A. JUNQUERA, ROBERTO R. HERENCIA, MANUEL MORALES, FRANCISCO M. REXACH, JUAN J. BERMÚDEZ, MARIA L. FERRÉ, WILLIAM J. TEUBER, JOSE R. VIZCARRONDO, FREDERIC V. SALERNO, MICHAEL J. MASIN, AND PRICEWATERHOUSE COOPERS, LLP, Defendants, and POPULAR, INC., a Puerto Rico Corporation, Nominal Defendant.	)	CIVIL ACTION NO. 3:09-cv-01507 JURY TRIAL DEMANDED

AMENDED VERIFIED SHAREHOLDER DERIVATIVE COMPLAINT FOR BREACH OF FIDUCIARY DUTY, GROSS MISMANAGEMENT, CORPORATE WASTE AND UNJUST ENRICHMENT

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Plaintiff Ruben Garcia, by and through the undersigned attorneys, derivatively on behalf of Popular, Inc. ("Popular" or the "Company"), alleges as follows, upon personal knowledge as to himself and his own acts, and upon information and belief as to all other matters, based upon, *inter alia*, the investigation conducted by and through his attorneys, which included, among other things, a review and analysis of: Popular's public filings with the U.S. Securities and Exchange Commission ("SEC"), news reports, press releases, information obtained from confidential informants and other lawsuits by investors and employees.

NATURE OF ACTION

1. This is a shareholder derivative action brought by Plaintiff, a stockholder of record of Popular, on behalf of Nominal Defendant, Popular, and all Popular shareholders against certain current and former executive officers (¶¶ 41-43), members of the Company's Board of Directors (identified below at ¶¶ 32-40 as "Director Defendants," and referred to collectively with the executive officers as the "Individual Defendants") and the Company's public accountants, Pricewaterhouse Coopers, which purportedly reviewed and certified all the SEC filings referred to herein (referred collectively with the Individual Defendants as "Defendants"). This derivative action arises from Defendants' breaches of their fiduciary duties of loyalty, candor and good faith, waste of Popular's corporate assets, and abuse of their control of Popular in connection with their causing, approving, and/or acquiescing in: (1) Popular's issuance of false and misleading financial reports and financial statements filed with the SEC that violated Generally Accepted Accounting Principles ("GAAP") by improperly accounting for nearly $1 billion in gross deferred tax assets that accumulated between the end of 2006 through 2008, causing the Company's earnings and capitalization to be inflated by hundreds of millions of dollars and making the Company appear as though it was "well-capitalized" as defined by the Federal Deposit Insurance Corporation ("FDIC") when in actuality it was undercapitalized; and (2) Popular's May 22, 2008 public offering of $400 million of non-cumulative perpetual preferred stock offering (the "Series B Offering") pursuant to a materially false and misleading registration statement that reported artificially inflated earnings

because Defendants allowed and/or caused the Company to improperly account for its deferred tax assets.

2. As evidenced herein, the ramifications of Defendants' actions and breaches of their fiduciary duties to the Company are evident. Popular has lost hundreds of millions of shareholder equity, delisted two classes of preferred stock, sold off numerous assets and has been forced to seek $950 from the U.S. Department of the Treasury's Capital Purchase Program under the Troubled Assets Relief Program ("TARP"). Despite all of these events, certain Individual Defendants were paid over a million dollars in incentive compensation directly tied to Popular's financial results, which were falsely reported in violation of GAAP.

3. Popular, is a publicly owned bank holding company incorporated in 1984 under the laws of the Commonwealth of Puerto Rico and is the largest financial institution based in Puerto Rico. Popular operates in multiple international jurisdictions including Puerto Rico, the U.S., Venezuela and the Dominican Republic. Popular's Puerto Rico operations ("Popular PR") primarily provide retail and commercial banking services through Banco Popular de Puerto Rico. Before the massive downsizing that was announced in January 2007 and essentially completed by late 2008, Popular's United States operations ("Popular U.S.") primarily consisted of Banco Popular North America ("BPNA"), a commercial bank; Popular Financial Holdings ("PFH"), a consumer finance company; and E-LOAN, an online consumer lending company. The Company also operated processing and other technology services in Venezuela and the Dominican Republic.

4. However, beginning at least as early as March 1, 2007, the day the Company filed its 2006 Form 10-K with the SEC, and continuing through the present (the "Relevant Period"), Individual Defendants in breach of their fiduciary duties, devised, approved and implemented a plan to unlawfully and unethically allow the Company to improperly account for its deferred tax assets related to Popular U.S. Specifically, for the years ending December 31, 2006 through 2008, Popular's recorded gross deferred tax assets grew from $437 million to $1.351 billion, a 209% increase, however, the Company failed to record any meaningful valuation allowances against this ballooning asset as required under GAAP until the third quart of 2008. A valuation allowance is

required by GAAP because of the highly speculative nature of these assets, the recoverability of which is dependent on future events. Indeed, under GAAP, Popular was required to record a full valuation allowance for its Popular U.S. deferred tax assets because the Company's U.S. operations were not "more likely than not" to realize the benefit of those assets.

5. Deferred tax assets are operating losses, tax credits and future tax deductions that can be used to offset taxable income in future years, if that taxable income materializes. Deferred tax assets can be used in the future to reduce a company's future tax payments by offsetting the temporary differences comprising the deferred tax asset against future taxable income. The GAAP standards for accounting for deferred tax assets are set forth in the SFAS No. 109, "Accounting for Income Taxes" ("SFAS 109"). While SFAS 109 requires a company to recognize all of its deferred tax assets, it requires a company to reduce the value of its deferred tax assets with a valuation allowance if it is "more likely than not" that some or all of the deferred tax assets will not reduce future taxable income. Recognizing a deferred tax asset that is not expected to be realized without recording a valuation allowance is prohibited because failing to reduce deferred tax assets artificially inflates a company's earnings. According to SFAS 109, ¶ 20, evidence to consider in determining whether a valuation allowance is required includes, among other things, a company's financial results for recent prior years, its current financial position, and currently available information about future years. Taking this information into account, to the extent a company can prove that future income will materialize, it is not required to record a valuation allowance; however, if a company cannot reliably prove that future taxable income will materialize, it must record a valuation allowance to the extent of the taxable income that is not "more likely than not" to materialize."

6. Here, amid an unprecedented economic downturn that crippled the financial and housing markets, both of which were critical to Popular U.S.'s success, Popular U.S.'s income started to steadily decrease since as early as 2005, culminating in a $645 million pre-tax loss in 2007. According to Confidential Witness ("CW1"), the Company knew it would take another larger loss in 2008, which it did by recording a $410 million pre-tax loss for fiscal year 2008. Furthermore, in the wake of rising delinquency rates on U.S. mortgages, Popular began to recognize increasing loan

losses as early as 2006. With no signs of the economy turning around any time soon, in January 2007, Popular announced and began downsizing a substantial portion of its Popular U.S. operations in January 2007. This further limited Popular U.S.'s ability to earn the future taxable income necessary to recover its deferred tax assets. Understanding that Puerto Rico PR and Popular U.S. operations (BPNA, E-LOAN and PFH) were suffering increasing losses, Individual Defendants decided not to reduce the carrying value of its deferred tax asset by recording a valuation allowance as required by GAAP to inflate its earnings. This allowed the Individual Defendants to trick the public and the FDIC into thinking that Popular was "well-capitalized." In reality, however, Popular was undercapitalized during the Relevant Period. Had Individual Defendants recorded proper valuation allowances, under FDIC regulations, Popular would have been prohibited from engaging in certain key operations, including non-banking activities and brokered deposit activities. To avoid this restriction, the Individual Defendants embraced a deferred tax strategy that would enable the Company to artificially inflate its earnings and to appear "well-capitalized."

7. In this case, the Individual Defendants either knew or recklessly disregarded that Popular would not earn future taxable income from its U.S. operations and failed to record a valuation allowance against its U.S. deferred tax assets. By failing to record a valuation allowance against nearly a $1 billion increase in gross deferred tax assets from Popular U.S. as required by GAAP, the Individual Defendants allowed and/or caused the Company to materially overstate its deferred tax assets, and thereby artificially inflate its GAAP earnings and capitalization by hundreds of millions of dollars during the Relevant Period. Having allowed and/or caused the Company to file materially false and misleading financial statements with the SEC in violation of state and federal securities laws, the Individual Defendants have exposed the Company to several lawsuits and investigations that could greatly diminish its assets. Indeed, the Company's share price has declined over 50% from its high in April 2007.

8. Under GAAP, Popular was required to record a valuation allowance if it was "more likely than not" that Popular U.S. would not generate sufficient future taxable income to realize the benefit of these deferred tax assets. Indeed, Popular confirmed in its 2006 and 2007 Form 10-Ks

acknowledge that this is its policy. However, the Individual Defendants, in particular, the Director Defendants who were members of the Audit Committee, two of which were designated as "financial experts," failed to conduct even a cursory review of the Company's financial statements and U.S. business prospects – a review which would have revealed that there was no credible basis for representing that Popular U.S. was capable of generating enough future taxable income to realize the deferred tax assets it reported.

9. Specifically and in violation of GAAP, it was clear that Popular U.S. was not "more likely than not" to realize its deferred tax assets based on the significant weight of negative evidence, or "red flags," available to Individual Defendants including:

> (i) In January 2007, the Company began to downsize, restructure and sell poorly performing Popular U.S. operations, including PFH, Equity One and E-LOAN, which significantly limited Popular U.S.'s ability to produce the future taxable income necessary to realize the deferred tax assets it had recorded. The restructuring of the Company's consolidated U.S. operations left Popular virtually incapable of producing the future taxable income necessary to allow Popular to realize all of the benefits from its deferred tax assets, which therefore required a significant valuation allowance;
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> (ii) Popular U.S. faced steadily deteriorating income since 2005. Indeed, according to Popular's December 31, 2007 Form 10-K, Popular U.S.'s pretax income (loss) for the years ending December 31, 2005, 2006 and 2007 decreased from $171 million to $10 million to a $(645) million loss, respectively, representing a three-year cumulative loss of $(465). These cumulative losses made it apparent that the Company could not produce sufficient future taxable income to recover its deferred tax assets;
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> (iii) Popular U.S.'s earnings in 2005, 2006 and 2007, as detailed *above* at ¶ 9(ii), represented a three-year cumulative loss of roughly $(465) million. According to SFAS 109, ¶103, "[a] cumulative loss in recent years is a significant piece of negative evidence that is difficult to overcome." There was simply no "positive evidence" that would overcome this cumulative loss evidence, as required by SFAS 109, ¶25 to support a conclusion that a valuation allowance was not required; and
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> (iv) Beginning in 2006 and through 2008, the fallout of the U.S. housing market caused the Company to increase its loan loss reserves. Popular U.S.'s construction and loan portfolios continued to deteriorate as the quality of its U.S. mortgages declined and the number of non-performing loans continued to increase. The increase in its loan loss reserve and the

continued deterioration of its U.S. loan portfolios were clear red flags that Popular U.S. had no realistic prospects for earning future taxable income.

10. The Director Defendants, in particular, were reckless and breached their fiduciary duties by ignoring these red flags. There was no indication, whatsoever, that Popular U.S. would recognize a profit in the foreseeable future. The Individual Defendants failed to question the Company's lack of any positive evidence, in light of the significant aforementioned negative evidence, that supported a conclusion that a valuation allowance was not required. Based on the negative evidence, pursuant to GAAP, the Company was required to record a valuation allowance against its deferred tax assets since at least the beginning of 2007 in its December 31, 2006 Form 10-K. Individual Defendants, however, recklessly disregarded these negative facts and continued to record deferred tax assets for Popular U.S. operations without recording the required valuation allowances, thereby inflating reported earnings and capital.

11. During the first two quarters of 2008, Individual Defendants sought to justify not recording a significant valuation allowance against its U.S. operations' deferred tax assets by relying solely on the fact that, under U.S. tax law, those assets had a standard expiration term of 20 years or longer. The Company's justification was improper under GAAP because the standard 20-year expiration term for net operating loss carryforwards ("NOL carryforward") provided in the U.S. tax code does not demonstrate that Popular will be "more likely than not" to earn sufficient taxable income to be able to realize the benefit of its deferred tax assets. The 20-year NOL carryforward period is simply the first prong of the test and provides an opportunity for an entity to carryforward past losses to offset future taxable income. In addition to the availability of the 20 year carryforward period, the Individual Defendants must satisfy a second prong; they have an affirmative duty to demonstrate that Popular U.S. has the capacity to generate future taxable income of the type that will allow it to utilize the potential benefits of the NOL carryforward. The absence of either prong negates recognition of a deferred tax asset.

12. Given all the specific red flags identified above, the Individual Defendants breached their fiduciary duties to the Company and acted recklessly or with gross negligence by allowing

Popular to advance and continue the flawed deferred tax asset strategy. Indeed, in light of all the negative information which was available to Defendants, it was not credible to assume that Popular U.S. would have the capacity to generate sufficient future taxable income to realize the benefit of its deferred tax assets. As previously stated, GAAP requires proof of an entity's ability to produce future taxable income when recognizing deferred tax assets. The Defendants failed to perform the appropriate due diligence to prove, or even test, the assumptions for either element.

13. Although the Individual Defendants continued to ignore these conspicuous red flags and failed to record proper valuation allowance as the deferred tax assets continued to increase significantly, Popular's dubious accounting concerning its deferred tax assets did catch the attention of Sterne Agee & Leach, Inc. ("Sterne Agee"), a securities analyst firm. In a July 22, 2008 report, Sterne Agee stated that "Popular's deferred tax asset (DTA) was a staggering $808 million in 2Q, up from $694 million in 1Q and $525 million in 4Q08. This 'asset' now totals nearly 27% of tangible equity (preferreds included). While we think Popular will be able to utilize a large portion of DTA over time, we continue to question the viability of the U.S. related portion of this asset."

14. At last, on October 22, 2008, Individual Defendants conceded that due to a three-year cumulative U.S. loss position, the Company was required to record a valuation allowance against Popular U.S.'s deferred tax assets. Individual Defendants explained in the Company's third quarter 2008 Form 10-Q filed on November 10, 2008, that the Company's $360.4 million valuation allowance followed a determination, albeit an incorrect determination, since the three-year cumulative loss occurred at least nine months earlier, that Popular U.S.'s operations were in a cumulative loss position as of September 30, 2008:

> The Corporation's U.S. mainland operations are in a cumulative loss position for the three-year period ended September 30, 2008. For purposes of assessing the realizibility of the deferred tax assets in the U.S. mainland, this cumulative loss position is considered significant negative evidence and has caused us to conclude that the Corporation will not be able to fully realize the deferred tax assets in the future.

15. Although Individual Defendants finally recognized that the Company had amassed a three-year cumulative loss, they were at least nine months late in recognizing the cumulative loss

and recording a valuation allowance. Indeed as discussed below, had the Individual Defendants recognized the cumulative loss, the Company would not have been able to go forward with the May 22, 2008 Series B Offering. As discussed above at ¶ 9(i)-(ii), the earnings for fiscal years 2005, 2006 and 2007 represented a three-year cumulative loss of roughly $465 million as of December 31, 2007. Therefore, pursuant to SFAS 109, Individual Defendants were required to record a valuation allowance in the Company's Form 10-K for fiscal year 2007 and the fourth quarter of 2007.

16. In addition, in the same 3Q 2007 Form 10-Q, the Individual Defendants attempted to justify their failure to record a full valuation allowance by claiming that the Company had adopted two purported tax strategies, which included transferring U.S. debt to the Puerto Rico operations and transferring a profitable line of business to the U.S. mainland operations.

17. These tax strategies, however, did not satisfy SFAS 109, ¶ 22 because the strategies lacked sufficient details, including what debt or profitable lines of business were involved, what benefits they would provide, what the costs would be, how Popular's management was in control of these strategies or how Popular could possibly obtain regulatory approval for these changes. Within a few months of the Company's feigned attempt to justify its failure to record an appropriate valuation reserve, the Company abandoned these alleged "tax strategies" confessing, as defendant Junquera admitted on a March 4, 2009 conference call, "we had to confront reality toward the end of last year."

18. Furthermore, because Defendants failed to perform proper due diligence or prevent the Company from recording its U.S. deferred tax assets without an appropriate valuation allowance, on May 22, 2008, the Individual Defendants allowed and/or caused the Company to engage in the Series B Offering – which sold approximately 16,000,000 shares of its 8.25% Non-cumulative Monthly Income Preferred Stock, Series B to the investing public at $25 per share, raising net proceeds of approximately $386,150,000. This Offering was predicated upon on a false and misleading prospectus filed with the SEC. Popular stated that the net proceeds were going to be used to for "general corporate purposes, which may include increasing the liquidity and capital of Popular, Inc. for their general corporate purposes, including the repayment of indebtedness or

19. Defendant Pricewaterhouse Coopers, LLP ("PwC") was unjustly enriched during the Relevant Period because it was compensated for issuing a clean, unqualified audit opinion on the Company's financial statements for the years ending December 31, 2006, 2007 and 2008, and allowed the quarterly Form 10-Q reports for the related interim periods to be filed without objection and/or adequate review, even though a proper valuation allowance on Popular U.S.'s deferred tax assets was not recorded, and in consenting to the inclusion of its opinion in the Series B Offering Documents, PwC failed to conduct its audit of Popular in a reasonable manner; did not comply with Generally Accepted Auditing Standards ("GAAS"); did not comply with standards of the Public Company Accounting Oversight Board ("PCAOB"); did not comply with PwC's own published audit guidance ("Accounting for Income Taxes"); and its audit did not constitute a reasonable investigation of whether the Company's financial statements were presented in compliance with GAAP.

20. On November 18, 2008, Popular was forced to announce it had had to seek government funds from TARP. As a result, Popular would be forced to issue and sell the U.S. Treasury $950 million worth of newly issued shares of preferred equity stock. In the Company's release that day, Individual Defendant Carrión now conceded that the TARP investment was required "to improve[] the liquidity and capital position of Popular" so that it could continue to "meet the needs of [its] customers and communities in the current challenging economic environment."

21. Finally, on January 22, 2009, Individual Defendants revealed that the Company would take a ***full*** valuation allowance of $861 million of Popular U.S.'s deferred tax assets. On this

news, the price of Popular securities plummeted. Specifically, the price of Popular common stock declined in one trading day by approximately 50%, from $4.98 to $2.46, and the Company lost over 50% of its market capitalization. During the Relevant Period, the stock traded as high as $17.11 on May 11, 2007. The valuation allowance caused the collapse of the Company's capital base forcing the Company on February 19, 2009, to cut its dividend by 75% to preserve its dwindling capital and enhance its liquidity. As a result, Popular's common stock again fell 11% in a single day, from $1.79 to $1.59, and Popular's Series B stock fell 43% in a single day, from $14 to $8.

22. Then on September 18, 2009, the Individual Defendants allowed and/or caused Popular to announce that it would delist its Series A and Series B preferred stock from Nasdaq.

23. By allowing the Company to file false and misleading financial statements throughout the Relevant Period and prospectus in connection with Popular's Series B Offering, Defendants exposed Popular to hundreds of millions of dollars in liability; all to the detriment of its shareholders. In fact, all Director Defendants are named as defendants, along with the Company itself, in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG, a securities fraud class action, and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both before this Court and include allegations concerning not only the GAAP violations and improper accounting of the deferred tax assets, but also the false and misleading Series B Offering.

24. This action seeks redress for the Individual Defendants' collective and individual breaches of their fiduciary duties of loyalty, good faith and candor, and their knowing, reckless and/or gross negligence in, *inter alia*: (i) failing to properly account for Popular U.S.'s deferred tax assets; (ii) allowing a false and misleading prospectus, which incorporated Defendants' flawed tax strategy and corresponding inflated earnings, to be filed with the SEC in connection with the Company's Series B Offering; (iii) failing to properly implement, oversee and maintain appropriate and adequate accounting and business ethics, internal controls, practices and procedures; and (iv) harming the value of the Company by the illegal and wrongful conduct engaged in by the Individual Defendants.

25. The Individual Defendants, in particular the Director Defendants who were on the Audit Committee, and Director Defendants Salerno and Teuber, who were designated as the financial experts of the Audit Committee for, among other things, their understanding of GAAP and internal controls over financial reporting, were on notice about the GAAP regulations regarding accounting for deferred tax assets. Despite the numerous "red flags" concerning the deteriorating business prospects of Popular U.S. and its inability to produce income in the foreseeable future, Director Defendants ignored those "red flags" and caused and/or allowed the Company to violate GAAP and expose the Company to significant losses and liabilities.

26. Individual Defendants' malfeasance has caused, and will continue to cause, Popular and its shareholders great harm by: (i) artificially maintaining Popular as "well-capitalized" by improperly accounting for Popular U.S.'s deferred tax assets, which when the truth was revealed, has caused the Company to increase capital; (ii) indelibly damaging its reputation and loss of goodwill in general; (iii) exposing the Company to potential criminal and civil liability, including suits for violations of securities laws and ERISA; (iv) having the Company absorb financial losses related to defense costs of cases brought by investors and employees; and (v) having the Company absorb the financial losses as the common stock price fell from its artificially inflated prices during the Relevant Period to a considerably lower price because of a "liars' discount" and a skepticism of its business operation by the investing public as a direct result of the Defendants' unlawful, unethical, and deceptive manner of handling their accounting responsibilities.

JURISDICTION

27. This Court has jurisdiction pursuant to 28 U.S.C. § 1332 because Plaintiff and Defendants are citizens of different states and the matter in controversy exceeds $75,000, exclusive of interest and costs. This action is not a collusive action designed to confer jurisdiction on a court of the United States that it would not otherwise have.

28. This court has jurisdiction over the subject matter of this action pursuant to 28 U.S.C. § 1331, because, as Defendants conceded (*See* Dkt. # 48 at 6 n.6), this is a civil action arising under the laws of the United States.

29. Venue is proper in this Court because one or more of the Defendants either resides in or maintains offices in this District, a substantial portion of the transactions and wrongs complained of herein, including the Defendants' primary participation in the wrongful acts detailed herein and aiding and abetting and conspiracy in violation of fiduciary duties owed to Popular occurred in this District, and Defendants have received substantial compensation in this District by doing business here and engaging in numerous activities that had an effect in this District.

THE PARTIES

A. Plaintiff

30. Plaintiff Ruben Garcia, is and was, a shareholder of nominal defendant Popular at relevant times. Plaintiff is a resident and citizen of the State of Florida.

B. Nominal Defendant

31. Nominal Defendant Popular, Inc. is a Puerto Rico corporation headquartered in San Juan, Puerto Rico. Popular is a publicly owned bank holding company registered under the Bank Holding Company Act of 1956, as amended and, accordingly, subject to the supervision and regulation of the Board of Governors of the Federal Reserve System. Popular was incorporated in 1984 under the laws of the Commonwealth of Puerto Rico and is the largest financial institution based in Puerto Rico, with consolidated assets of $38.9 billion, total deposits of $27.6 billion and stockholders' equity of $3.3 billion at December 31, 2008. As of December 31, 2008, Popular ranked 29th among bank holding companies based on total assets according to the Federal Reserve System. Popular operates and controls subsidiaries in three target markets: Puerto Rico, the United States, and processing and other technology services in Puerto Rico, Venezuela, Florida and the Dominican Republic. The Company offers retail and commercial banking services in Puerto Rico, through its principal bank subsidiary, Banco Popular de Puerto Rico. The Bank accounted for 66% of the total consolidated assets of the Company at December 31, 2008. Banco Popular has the retail franchise in Puerto Rico, with 179 branches and over 600 automated teller machines (ATMs). The Bank also operates seven branches in the United States Virgin Islands, one branch in the British Virgin Islands and one branch in New York. Banco Popular has two subsidiaries: Popular Auto,

Inc., a vehicle financing, leasing and daily rental company, and Popular Mortgage, Inc., a mortgage loan company with 32 offices in Puerto Rico. The Company has over 282 million shares of common stock issued and outstanding which trade on the Nasdaq under the ticker symbol "BPOP."

C. Director Defendants

32. Defendant Richard Carrión ("Carrión"), a resident and citizen of Puerto Rico, has been Chairman of the Board of Popular since 1993, CEO of Popular since 1994, formerly served as President of Popular from 1991 to January 2009, and has served as Chairman of the Bank since 1993, as CEO of the Bank since 1989, and formerly served as President of the Bank from 1985 to 2004. Carrión also serves as Chairman and CEO of Popular North America, Inc. and other direct and indirect wholly-owned subsidiaries of the Company. Carrión is recognized as an inside Director of the Company. Carrión has served as a Director of the Federal Reserve Bank of New York since January 2008. Carrión has also served as Chairman of the Board of Trustees of Fundación Banco Popular, Inc. since 1982 and as Chairman and Director of Banco Popular Foundation, Inc. since 2005. Carrión prepared, authorized and/or issued the false and misleading statements Popular made during the Relevant Period and signed false and misleading Sarbanes-Oxley certifications in connection with all of Popular's Relevant Period financial filings with the SEC. Carrión received over $2 million in salary, bonus and incentive compensation from Popular in fiscal 2008. As of January 20, 2009, Carrión was the beneficial owner of 3,264,174 of Popular's common stock, which represents 1.16% of the outstanding shares. Carrión also owns 11,156 shares of preferred stock. In 2006, Defendant Carrión's total compensation was $3,294, 206, of which $772, 650 was in salary and bonus and $178,139 was in performance incentives (including $148,320 in short-term incentives). In 2007, Defendant Carrión's total compensation was $2,475,628, of which $772, 655 was in salary and bonus and $25,779 was in performance incentives. In 2008, Defendant Carrión's total compensation was $1,395,622, of which $772, 660 was in salary and bonus.

33. Defendant Juan J. Bermúdez ("Bermúdez"), a resident and citizen of Puerto Rico, has served as a Director of Popular since 1990 and has served as Chairman of the Trust Committee of the Bank since 1996. During the Relevant Period, Bermúdez served as a member of the Audit

Committee and Compensation Committee. As of August 20, 2009, Bermúdez was the beneficial owner of 2,046,271 shares of Popular's common stock and, as of January 20, 2009, owns 63,600 shares of preferred stock. Defendant Bermúdez signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering.

34. Defendant Maria L. Ferré ("Ferré"), a resident and citizen of Puerto Rico, has served as a Director of Popular since April 2004. During the Relevant Period, Ferré served as a member of the Compensation Committee. As of January 20, 2009, Ferré was the beneficial owner of 6,560,044 shares of Popular's common stock, which represents 2.33% of the outstanding shares. Ferré also owns 4,175 shares of preferred stock. Defendant Ferré signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering.

35. Defendant Michael J. Masin ("Masin"), a resident and citizen of Florida, has served as a Director of Popular since January 2007. During the Relevant Period, Masin served as a member of the Risk Committee. As of January 20, 2009, Masin was the beneficial owner of 50,789 shares of Popular's common stock. Defendant Masin signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering.

36. Defendant Manuel Morales ("Morales"), a resident and citizen of Puerto Rico, has served as a Director of Popular since 1990. During the Relevant Period, Morales served as a member of the Risk Committee and the Compensation Committee. As of November 3, 2009, Morales was the beneficial owner of 92,803 shares of Popular's common stock. Defendant Morales signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering.

37. Defendant Francisco M. Rexach ("Rexach"), a resident and citizen of Puerto Rico, has served as a Director of Popular since 1990. During the Relevant Period, Rexach served as the

chairperson of the Compensation Committee and as a member of the Audit Committee. As of January 20, 2009, Rexach was the beneficial owner of 390,987 shares of Popular's common stock. Defendant Rexach signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering.

38. Defendant Frederic V. Salerno ("Salerno"), a resident and citizen of Florida, has served as a Director of Popular since 2003. During the Relevant Period, Salerno served as the chairperson and a financial expert, as defined by Item 407(d)(5) of Regulation S-K under the Securities Exchange Act of 1934, of the Audit Committee and served as a member of the Risk Committee. Salerno retired as Vice Chairman and CFO of Verizon, Inc. in September 2002 after more than 37 years in the telecommunications industry. Prior to the Bell Atlantic/GTE merger, which created Verizon, he was Senior Vice Chairman and CFO of Bell Atlantic and President and CEO of New York Telephone. As of January 20, 2009, Salerno was the beneficial owner of 74,534 shares of Popular's common stock. Defendant Salerno signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering.

39. Defendant William J. Teuber ("Teuber"), a resident and citizen of Massachusetts, has served as a Director of Popular since 2004. As of January 20, 2009, Teuber was the beneficial owner of 35,504 shares of Popular's common stock. During the Relevant Period, Teuber served as a financial expert, as defined by Item 407(d)(5) of Regulation S-K under the Securities Exchange Act of 1934, for the Audit Committee and served as the chairperson of the Risk Committee. Teuber serves as Vice Chairman of EMC Corporation since 2006 and was EMC's Executive Vice President since 2001 and CFO from 1997 to 2006. Defendant Teuber signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering.

40. Defendant Jose R. Vizcarrondo ("Vizcarrondo"), a resident and citizen of Puerto Rico, has served as a Director of Popular since 2004 and as a member of the Trust Committee of the Bank since 2004. During the Relevant Period, Vizcarrondo served as a member of the Risk Committee. As of November 3, 2009, Vizcarrondo was the beneficial owner of 212,107 shares of Popular's common stock and 12,000 shares of preferred stock. Defendant Vizcarrondo signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering.

D. <u>Officer Defendants</u>

41. Defendant David H. Chafey ("Chafey"), a resident and citizen of Puerto Rico, has served as Popular's President and Chief Operating Officer since January 2009. Chafey served as President of the Bank since 2004 and Supervisor of the Bank's Retail Banking Group from 1996 through 2004. Chafey has also served as Senior Executive Vice President of Popular International Bank, Inc. since 1999 and Popular North America, Inc. since 2000, direct and indirect wholly-owned subsidiaries of Popular. In 2006, Defendant Chafey's total compensation was $3,171,665, of which $726,693 was in salary and bonus and $434,474 was in performance incentives (including at least $174,375 in short-term incentives). In 2007, Defendant Chafey's total compensation was $2,299,508, of which $726,698 was in salary and bonus and $374,694 was in performance incentives (including $346,870 in short-term incentives). In 2008, Defendant Chafey's total compensation was $2,162,303, of which $793,994 was in salary and bonus.

42. Defendant Jorge A. Junquera ("Junquera"), a resident and citizen of Puerto Rico, has served as Popular's Senior Executive Vice President and Chief Financial Officer since 1997 and as a Director of Popular since 1990. Junquera also serves as Chief Financial Officer of the Bank and Supervisor of the Financial Management Group. Previously, Junquera served as Supervisor of the Popular, Inc. U.S. Operations from January 1996 to December 2001, and has served as President and Director of Popular International Bank, Inc. and Popular North America, Inc. since January 1996, directly and indirectly wholly-owned subsidiaries of the Popular, Inc, respectively. Junquera also

served as a Director of the Bank until April 2000 and from 2001 to present. Junquera served as President of Banco Popular North America until December 2001, as President of Banco Popular, National Association, a Director of Popular Financial Holdings, Inc., Popular Cash Express, Inc., Popular FS, LLP, Popular Leasing USA, Inc. and of Banco Popular North America, indirectly wholly-owned subsidiaries of the Corporation and serves as a Director of Banco Hipotecario Dominicano and Consorcio de Tarjetas Dominicanas, S.A., where Popular has an indirect investment. Junquera prepared, authorized and/or issued the false and misleading statements Popular made during the Relevant Period and signed false and misleading Sarbanes-Oxley certifications in connection with all of Popular's Relevant Period financial filings with the SEC. Defendant Junquera signed the Company's materially misstated Offering Documents through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering. In 2006, Defendant Junquera's total compensation was $1,239,298, of which $561,633 was in salary and bonus and $156,423 was in performance incentives (including at least $140,408 in short-term incentives). In 2007, Defendant Junquera's total compensation was $770,221, of which $561,638 was in salary and bonus and $153,487 was in performance incentives (including $134,750 in short-term incentives). In 2008, Defendant Junquera's total compensation was $801,232, of which $562,766 was in salary and bonus.

43. Defendant Roberto R. Herencia ("Herencia"), a resident and citizen of Illinois, served as President and Director of BPNA from 2001 until December 31, 2008. Herencia also served as Popular's Executive Vice President since 1997. On December 31, 2008, Defendant Herencia resigned as Executive Vice President of the Corporation and President of Banco Popular North America. On November 6, 2008, the Popular Board of Directors approved the Resignation and Transition Agreement with Defendant Herencia. Under the agreement, Herencia received a severance payment equal to $3,289,432, of which 85% was paid on November 12, 2008 and the remainder was paid on February 6, 2009. In addition, he received $42,875 corresponding to transition-related services performed during January 2009. Under the terms of the agreement, all restricted stock awards previously granted to Defendant Herencia vested immediately upon his

resignation. In 2006, Defendant Herencia's total compensation was $1,445,449, of which $510,491 was in salary and bonus and $257,160 was in performance incentives (including at least $122,500 in short-term incentives). In 2007, Defendant Herencia's total compensation was $1,089,883, of which $510,697 was in salary and bonus and $68,547 was in performance incentives (including $49,000 in short-term incentives). In 2008, Defendant Herencia's total compensation was $5,044,957, of which $534,138 was in salary and bonus.

44. The Director Defendants and Officer Defendants referenced above in ¶¶ 30-43 are referred to herein as the "Individual Defendants."

E. <u>Auditor Defendant</u>

45. Defendant Pricewaterhouse Coopers maintains its national headquarters in New York. PwC served as the Company's outside auditor at all relevant times, provided audit and tax services to the Company prior to and throughout the Relevant Period. PwC audited Popular's assessment of the effectiveness of the Corporation's internal control over financial reporting and certified all financial statements Popular filed during the Relevant Period, which improperly accounted for Popular U.S.'s deferred tax assets. PwC participated in the due diligence and consented to the incorporation by reference in the Offering Documents for the Series B Offering of its clean and unqualified audit opinion letter on the Company's financial statements and its opinion letter on management's assessment of internal controls for the years ended December 31, 2006, December 31, 2007, and December 31, 2008. For the year ended December 31, 2006, PwC was paid: (a) fees for audit services of approximately $3,486,500; (b) fees for other services, including compliance-related audit and accounting consulting, of approximately $754,000; and (c) fees associated with tax consulting services of approximately $150,000. For the year ended December 31, 2007, PwC was paid: (a) fees for audit services of approximately $4,462,593; (b) fees for other services, including compliance-related audit and accounting consulting, of approximately $1,280,792; and (c) fees associated with tax consulting services of approximately $150,000. For the year ended December 31, 2008, PwC was paid: (a) fees for audit services of approximately $4,563,000; (b) fees for other services,

including compliance-related audit and accounting consulting, of approximately $1,533,500; and (c) fees associated with tax consulting services of approximately $66,000.

46. Popular, the Director Defendants, the Individual Defendants and PwC are referred to herein collectively as the "Defendants."

SUBSTANTIVE ALLEGATIONS

A. Background

47. Popular is a bank holding company with operations in the U.S., Puerto Rico, Venezuela and the Dominican Republic. The Company operates in two main target markets: Puerto Rico (previously defined as "Popular PR") and the mainland United States (previously defined as "Popular U.S."). Throughout the Relevant Period, Popular PR offered retail and commercial banking services through its principal bank subsidiary, Banco Popular de Puerto Rico, Puerto Rico's largest bank. Popular U.S. offered retail and commercial banking services through Banco Popular North America (previously defined as "BPNA") and consumer finance services through Popular Financial Holdings, Inc. (previously defined as "PFH"). BPNA's operating subsidiaries included E-LOAN, a provider of online consumer direct lending. PFH's operating subsidiaries included Equity One, a subprime loan originator and provider of mortgage and consumer loans, and Popular Mortgage Servicing, Inc., a third-party mortgage servicing provider which housed Popular's manufactured housing loan portfolio.

48. Puerto Rico is classified by the U.S. government as an independent taxation authority by mutual agreement with the U.S. Congress. According to the Company's 2007 Form 10-K, "[t]he Corporation's U.S. subsidiaries . . . are considered foreign under Puerto Rico income tax law . . ." Hence, deferred tax assets accumulated by the Company from its Popular U.S. operations could only be realized by future profits earned from Popular U.S., and not from Popular PR.

B. The Individual Defendants' General Duties and Obligations

49. By reason of their positions as officers, directors and/or fiduciaries of Popular and because of their ability to control the business and corporate affairs of Popular, the Individual

Defendants owed Popular and its shareholders fiduciary obligations of care, candor, compliance, fidelity, trust, loyalty and due care, and were and are required to use their utmost ability to control and manage Popular in a fair, just, honest and equitable manner, and were and are required to act in furtherance of the best interests of Popular and its shareholders so as to benefit all shareholders equally and not in furtherance of their personal interest or benefit.

50. Each director and officer of the Company owes to Popular the fiduciary duty to comply with the laws of the United States and to exercise due care and diligence in the administration of the affairs of the Company and in the use and preservation of its property and assets, and the highest obligations of good faith and fair dealing.

51. In addition, as officers and/or directors of a publicly held company, the Individual Defendants had a duty to promptly disseminate accurate and truthful information with respect to the Company's finances and operations, so that the market price of the Company's stock would be based on truthful and accurate information. Individual Defendants also had an obligation not to entrench themselves as officers and/or directors of the Company, to allow open and honest board elections and to not advance their own personal, financial or economic interests over, and at the expense of, the Company's public shareholders.

52. The Individual Defendants, because of their positions of control and authority as directors or officers of Popular, were able to and did, directly and indirectly, control the wrongful acts complained of herein, as well as the contents of the various public statements issued by the Company. Because of their advisory, executive, managerial, and directorial positions with Popular, each of the Individual Defendants had access to all non-public information about the financial condition, operations and future business prospects of Popular, including, without limitation, the illegal and improper activities which the Individual Defendants caused Popular to engage in.

53. At all times relevant hereto, each of the Individual Defendants was the agent of each of the other Individual Defendants and of the Company, and was at all times acting within the course and scope of such agency.

54. To discharge their duties, the officers and directors of Popular were required to exercise reasonable and prudent supervision over the management, policies, practices and controls of the financial and operational affairs of Popular. By virtue of such duties, the officers and directors of Popular were required to, among other things:

(a) manage, conduct, supervise and direct the business and internal affairs of Popular in accordance with the laws and regulations of Puerto Rico, the United States, and pursuant to the charter and bylaws of Popular;

(b) neither violate, nor knowingly permit any officer, director or employee of Popular to violate applicable laws, rules and regulations;

(c) remain informed as to the status of Popular's operations, and upon receipt of notice or information of imprudent or unsound practices, to make a reasonable inquiry in connection therewith, and to take steps to correct such conditions or practices and make such disclosures as are necessary to comply with applicable laws and regulations;

(d) establish and maintain systematic and accurate records and reports of the business and internal affairs of Popular and procedures for the reporting of the business and internal affairs to the Board of Directors and to periodically investigate, or cause independent investigation to be made of, said reports and records;

(e) maintain and implement an adequate and functioning system of internal legal, financial and management controls, such that Popular's operations would comply with all laws, Popular's financial statements and information filed with U.S. financial regulators and disseminated to the investing public and to Popular shareholders in Annual Reports would be accurate and the actions of its directors would be in accordance with all applicable laws; and

(f) exercise reasonable control and supervision over the public statements to the securities markets, investors and public shareholders of Popular by the officers and employees of Popular and any other reports or other information required by law from Popular and to examine and evaluate any reports of examinations, audits or other financial information concerning the financial

affairs of Popular and to make full and accurate disclosure of all material facts concerning, *inter alia*, each of the subjects and duties set forth above.

55. During all times relevant hereto, each of the Individual Defendants occupied positions with Popular or was associated with the Company in such a manner as to make him or her privy to confidential and proprietary information concerning Popular, its operations, finances and financial condition. Because of these positions and such access, each of the Individual Defendants knew that the true relevant facts specified herein had not been disclosed to and were concealed from Popular's shareholders. The Individual Defendants, as corporate fiduciaries entrusted with non-public information, were obligated to disclose material information regarding Popular and to take any and all actions necessary to ensure that the officers and directors of Popular did not abuse their privileged positions of trust, loyalty and fidelity in a manner which caused the Company to violate the law.

56. The conduct of the Individual Defendants complained of herein involves a knowing and culpable violation of their obligations as directors and officers of the Company, the absence of good faith on their part, and a reckless disregard for their duties to the Company and its shareholders that Individual Defendants were aware or should have been aware posed a risk of serious injury to the Company. The conduct of the Individual Defendants who were also officers and/or directors of the Company during the Relevant Period has been enabled and ratified by the remaining Director Defendants who comprise a majority of the Company's Board during the Relevant Period.

C. <u>Popular's Code of Ethics</u>

57. Popular maintains a corporate governance section on its website, www.popular.com, where investors may find copies of its principal governance documents. The corporate governance section of the Company's website contains, among others, a Code of Ethics (the "Code") that the Board has adopted to be followed by the Company's employees, officers (including the CEO, CFO, COO and Corporate Comptroller) and directors to achieve conduct that reflects the Corporation's ethical principles.

58. Certain portions of the Code deal with activities of directors, particularly with respect to transactions in the securities of the Company and potential conflicts of interest. Directors,

executive officers and employees are required to be familiar with and comply with the Code. The Code provides that any waivers for executive officers or directors may be made only by the independent members of the Board and must be promptly disclosed to the stockholders. According to the Company, during 2008, Popular did not receive or grant any request from directors or executive officers for waivers under the provisions of the Code.

As to Disclosure of Financial Information, Popular's Code states:

> Financial statements must always be prepared in accordance with generally accepted accounting principles and fairly illustrate, in all material respects, Popular's financial condition and results. Furthermore, Popular is committed to preparing and maintaining accurate tax-related records, and to submitting tax reports and returns, as well as paying taxes, on a timely basis and in compliance with all applicable laws.
>
> ***
>
> Popular makes, through our senior financial officers, full, fair, accurate, timely and understandable disclosure of information that must be made public pursuant to federal securities laws.
>
> Employees and directors involved in the disclosure process of Popular's financial information are required to be familiar and comply with this Code, the disclosure controls and procedures, and all internal controls over financial reporting procedures. These individuals must also: (a) be aware of the disclosure requirements applicable to Popular, as well as of the business and financial operations of Popular; (b) not knowingly misrepresent, or cause others to misrepresent, facts about Popular, whether within or outside Popular, including to Popular's independent auditors, governmental regulators and self-regulatory organizations; (c) not take any action to fraudulently coerce or manipulate our independent auditors in any way that could render our financial statements misleading; and (d) properly review and critically analyze proposed disclosures for accuracy and completeness (or, where appropriate, delegate this task to others).
>
> Popular is committed to fully comply with the Securities and Exchange Commission's regulations pertaining to disclosure of information, including Regulation FD (Fair Disclosure). To ensure compliance with such Regulation, employees must consult with the Corporation's Chief Financial Officer prior to arranging or participating in any investor or analyst meeting.

D. <u>Duties and Responsibilities of Committees of the Board</u>

59. Two standing committees of the Board include the Audit Committee and the Compensation Committee.

1. Audit Committee

60. The following Director Defendants served on the Audit Committee of the Popular Board of Directors during the Relevant Period: Bermúdez, Rexach, Salerno (financial expert) and Teuber (Chairperson and financial expert).

61. The Audit Committee held eleven meetings during 2008 and Company earnings releases, Form 10-K and Form 10-Q filings were discussed in eight of such meetings. During 2007, the Audit Committee held eleven meetings and Company earnings releases, Form 10-K and Form 10-Q filings were discussed in eight of such meetings. During 2006, the Audit Committee held thirteen meetings and Company earnings releases, Form 10-K and Form 10-Q filings were discussed in ten of such meetings.

62. The Audit Committee's primary purpose is to assist the Board in its oversight of the accounting and financial reporting processes of the Company. The Audit Committee operates pursuant to a charter that was last amended and restated by the Board on December 19, 2007.

63. Among other things, Popular's Audit Committee charter charged its members with: (i) overseeing the integrity of Popular's financial statements, including policies, procedures and practices regarding the preparation of financial statements, the financial reporting process, disclosures, and the internal control over financial reporting; (ii) overseeing Popular's internal audit function and the qualifications, independence and performance of its outside auditors; and (iii) investigating any matters brought to its attention or initiated on its own and that it was provided full access to all of the Company's books, records and personnel of the Company.

64. To be designated financial experts, Director Defendants Salerno and Teuber had to meet specific qualifications. According to Item 407(d)(5)(ii) of Regulation S-K under the Securities Exchange Act of 1934, an audit committee financial expert, such as Salerno and Teuber, means a person who has the following attributes: (i) an understanding of generally accepted accounting principles (GAAP) and financial statements; (ii) the ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves; (iii) experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of

complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrants' financial statements, or experience actively supervising one or more persons engaged in such activities; (iv) an understanding of internal control over financial reporting; and (v) an understanding of audit committee functions.

65. As the Audit Committee's financial experts throughout the Relevant Period, Director Defendants Salerno and Teuber would have understood that Popular's deferred tax strategy was improper and that it violated GAAP. Salerno and Teuber were responsible for preventing the Company from taking these improper actions, which they failed to do.

66. As described herein, the above-referenced responsibilities were violated by Director Defendants Bermúdez, Rexach, Salerno and Teuber as members of the Audit Committee during the Relevant Period, and as such, each faces a substantial likelihood of liability by this action. Bermúdez, Rexach, Salerno and Teuber continue to serve on Popular's Board, and are disabled from performing a disinterested view of the claims in this case, and from acting to bring a suit and remedy the wrongs described herein.

2. Compensation Committee

67. The following Director Defendants served on the Audit Committee of the Popular Board of Directors during the Relevant Period: Bermúdez, Ferré, Morales, Rexach (Chairperson) and Teuber.

68. The Compensation Committee held five meetings in 2006, 2007 and 2008.

69. The purpose of the Compensation Committee is to discharge the Board's responsibilities (subject to review by the full Board) relating to compensation of the Company's executives and to produce an annual report on executive compensation for inclusion in the Company's proxy statement, in accordance with the rules and regulations of the SEC. In addition, since 2008, the Compensation Committee reviews and assesses incentive compensation arrangements to ensure that they do not encourage senior executive officers to take unnecessary and excessive risks that may threaten the value of the Company.

70. Among other things, Popular's Compensation Committee charter charges its members with overseeing Popular's compensation policies and practices, including designing and implementing adequate insider trading provisions, to ensure that Popular's executives are not incentivized to operate the Company in a reckless fashion or to take on undue risk in the race to report financial results that directly influence their own compensation.

71. The above-referenced responsibilities were violated by Director Defendants Bermúdez, Ferré , Morales, Rexach and Teuber as members of the Compensation Committee during the Relevant Period, and as such, each faces a substantial likelihood of liability by this action. Specifically, the Compensation Committee members encouraged the Individual Defendants, in particular, executive defendants Carrión, Chafey, Junquera and Herencia, to violate GAAP by improperly accounting for Popular U.S.'s deferred tax assets, and thereby inflating the Company's earnings, through its "Short-Term Incentive[s]" program for the Company's senior executives. The short-term cash incentives were designed to reward achievement of annual profit goals and reflect the senior executive's degree of control or influence over the Corporation's and individual business unit results. These cash rewards provided the Individual Defendants with incentives to inflate their business unit's earnings.

72. Despite the fact that Popular U.S. was experiencing significant losses and Popular was undercapitalized, the Compensation Committee continued to award executive defendants Carrión, Chafey, Junquera and Herencia cash bonuses based on their short-term incentive program. For instance, in 2006, the Compensation Committee approved an award of 20% of Carrión's base pay, or $148,320, and awards of between 25-30% of Chafey, Junquera and Herencia's base salaries, even though the Company was improperly accounting for its deferred tax assets.

73. In 2007, the Compensation Committee did not award Carrión a short-term incentive because:

> 2007 was a very difficult year for the Corporation's business in the United States, Popular North America, Inc., and its results of operations for 2007 was considerably below the pre-established threshold. This was mainly due to losses suffered as a result of extremely difficult mortgage and credit markets, Popular Financial Holdings, Inc. restructuring plans and loan recharacterization transaction and the

> restructuring plan at E-LOAN, Inc. which led to goodwill and trademark impairments. Popular North America's financial difficulties had a significant impact on the Corporation's results of operations. The Corporation experienced a 2007 net loss of approximately $64.5 million and, therefore, did not reach the minimum performance threshold of approximately $344 million of net profit.

74. Although the Compensation Committee refused to approve Carrión's short-term incentive for the reasons above, in 2007, the Compensation Committee inexplicably granted Herencia an award of 10% of his base salary, or $49,000, for purportedly integrating BPNA, PFH and E-LOAN "into one management entity, Popular North America, and executing several difficult strategic initiatives aimed at improving the deteriorating profitability resulting from the subprime crisis, the ongoing decline in the real estate market and the credit liquidity crisis." The Compensation Committee also granted Junquera an award of 25% of his base salary, or $134,750, "for their significant contributions in his specific areas of expertise to the numerous complex strategic initiatives and restructurings that took place during 2007." The Compensation Committee also granted Defendant Chafey an award of 20% of his base salary, or $346,870, for among other things "***utilizing effective cost efficiency measures to counteract the negative income impact of increases in the loan loss provision***." (Emphasis added.) The Compensation Committee granted these short-term incentives , as further detailed below, in spite of the fact that the Individual Defendants were downsizing BPNA, PFH and E-LOAN due to poor performance, Popular U.S. was suffering a three-year cumulative loss and the Company was increasing loan loss reserves due to the housing market collapse. By granting these short-term incentives, the Compensation Committee encouraged the Individual Defendants to find creative measures to make their business units, and the overall Company, appear more successful than it actually was.

75. Furthermore, as detailed above at ¶¶ 32, 41-43, the Compensation Committee approved of salary increases for executive defendants Carrión, Chafey, Junquera and Herencia, knowing that Popular U.S. was suffering ongoing losses and that Popular was undercapitalized.

76. In addition, the Compensation Committee improperly approved the Resignation and Transition Agreement with defendant Herencia, under which he received a severance payment equal to $3,289,432. This was an excessive and unwarranted award considering that Herencia was in

charge of BPNA and E-LOAN, which were virtually liquidated because of poor performance under Herencia's leadership.

77. The Compensation Committee also authorized the continued provision to Carrión of a corporate jet, non-work related security and a New York apartment for personal use, and the continued provision to Carrión, Chafey and Junquera of Company-owned vehicles, country club memberships, and tickets to sponsored events which admittedly cost Popular tens, if not hundreds, of thousands of dollars a year to provide.

78. Bermúdez, Ferré , Morales, Rexach and Teuber continue to serve on Popular's Board, and are disabled from performing a disinterested view of the claims in this case, and from acting to bring a suit and remedy the wrongs described herein.

79. The following chart reflects the years in which different Director Defendants served on these two standing committees during the Relevant Period:

AUDIT COMMITTEE				
Defendant	**2009**	**2008**	**2007**	**2006**
Bermúdez	Member	Member	Member	Member
Rexach	Member	Member	Member	Member
Salerno	Chair (Financial Expert)	Chair (Financial Expert)	Chair (Financial Expert)	Chair (Financial Expert
Teuber	Member (Financial Expert)	Member (Financial Expert)	Member (Financial Expert)	Member (Financial Expert

COMPENSATION COMMITTEE				
Defendant	**2009**	**2008**	**2007**	**2006**
Bermúdez	Member	Member	Member	Member
Ferré	Member	Member	Member	Member
Morales	Member			
Rexach	Chair	Chair	Chair	Chair
Teuber	Member	Member	Member	Member

E. Deferred Tax Accounting

1. The Role of the FASB

80. During the Relevant Period, publicly traded companies, such as Popular, are required to disclose financial information consistent with GAAP, as defined by the Financial Accounting Standards Board ("FASB"). As discussed above, Director Defendants, in particular, the members of the Audit Committee and Defendants Salerno and Teuber as financial experts, are expected to be familiar with GAAP and establish the necessary internal controls and oversight procedures required to ensure that the Company and its financial statements comply with GAAP.

81. The FASB is the designated organization in the private sector for establishing standards of financial accounting. Those standards govern the preparation of financial statements. These standards are officially recognized as authoritative by the SEC. SEC Regulation S-X (17 C.F.R. § 210.4-01(a)(1)) provides that financial statements filed with the SEC which are not presented in accordance with GAAP will be presumed to be misleading, despite footnotes or other disclosures.

82. In establishing the GAAP standards for financial accounting, FASB follows a process that is open to public observation and encourages public comment on proposed standards. After this process, the final product is a Statement of Financial Accounting Standards ("SFAS") that sets forth the actual standards, the effective date and method of transition, background information, a brief summary of research done on the project, and the basis for the Board's conclusions, including the reasons for rejecting significant alternative solutions collected during the public comment period.

2. SFAS 109 – "Accounting for Income Taxes"

83. SFAS No. 109, "Accounting for Income Taxes," published in 1992, sets forth the GAAP standards for accounting for deferred tax assets and liabilities. According to SFAS 109, "a deferred tax asset is recognized for temporary differences that will result in deductible amounts in future years and for carryforwards. For example, a temporary difference is created between the reported amount and the tax basis of a liability for estimated expenses if, for tax purposes, those estimated expenses are not deductible until a future year. Settlement of that liability will result in tax

deductions in future years, and a deferred tax asset is recognized in the current year for the reduction in taxes payable in future years."

84. Essentially, deferred tax assets are losses, credits and other tax deductions that can reduce further taxes payable resulting from taxable income in future years. Deferred tax assets can be used in the future to reduce a company's tax payments by offsetting the temporary differences comprising the current deferred tax asset against future taxable income. However, given the speculative and highly judgmental basis for deferred tax asset recognition, under SFAS 109, a company must affirmatively demonstrate that there is more than a 50% probability that the company will generate the future taxable income necessary to recover the deferred tax asset it records.

85. If it is "more likely than not" that some or all of the deferred tax assets will not be realized with future taxable income, under SFAS 109, a company must reduce the value of its gross deferred tax assets with a valuation allowance to reduce the carried value of its deferred tax asset to its realizable value. Recognizing a deferred tax asset that is not expected to be realized without reducing it with an appropriate valuation allowance is prohibited.

86. Specifically, SFAS 109, ¶ 17 states:

> Deferred taxes shall be determined separately for each tax-paying component (an individual entity or group of entities that is consolidated for tax purposes) in each tax jurisdiction. That determination includes the following procedures:
>
> ***
>
> (e) Reduce deferred tax assets by a ***valuation allowance*** if, based on the weight of available evidence, it is more likely than not (a likelihood of more than 50 percent) that some portion or all of the deferred tax assets will not be realized. The valuation allowance should be sufficient to reduce the deferred tax asset to the amount that is more likely than not to be realized.

(Emphasis original.)

3. The Significance of Negative Evidence on the Valuation Allowance

87. To determine whether it is more likely than not that a company will have sufficient future taxable income to avoid recording a valuation allowance, SFAS 109, ¶ 20 requires that:

> All available evidence, both positive and negative, should be considered to determine whether, based on the weight of that evidence, a valuation allowance is needed. Information about an enterprise's current financial position and its results of

> operations for the current and preceding years ordinarily is readily available. ***That historical information is supplemented by all currently available information about future years.***

(Emphasis added.)

88. SFAS 109 also provides guidance as to what constitutes negative evidence requiring a valuation allowance to be recorded. According to SFAS 109, ¶ 23 "[f]orming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years." Also, "[l]osses expected in the near future" by an entity and "unsettled circumstances that, if unfavorably resolved, would adversely affect future operations and profit levels on a continuing basis in future years" constitute negative evidence. SFAS 109, ¶ 23(b)-(c). In this case, Popular U.S. had significantly deteriorating results from 2005 forward and a cumulative three-year loss as early as the fourth quarter of 2007.

89. Furthermore, in Appendix A of SFAS 109 entitled "Basis for Conclusions," FASB states that "[a] cumulative loss in recent years is a significant piece of negative evidence that is difficult to overcome." SFAS 109, ¶ 103.

90. According to SFAS 109, ¶ 25:

> An enterprise must use judgment in considering the relative impact of negative and positive evidence. The weight given to the potential effect of negative and positive evidence should be commensurate with the extent to which it can be objectively verified. ***The more negative evidence that exists (a) the more positive evidence is necessary and (b) the more difficult it is to support a conclusion that a valuation allowance is not needed for some portion or all of the deferred tax asset***.

(Emphasis added.)

91. "[The above] criterion requires positive evidence of sufficient quality and quantity to counteract negative evidence in order to support a conclusion that, based on the weight of all available evidence, a valuation allowance is not needed." SFAS 109, ¶103. During the Relevant Period, Popular did not possess or provide any "positive" evidence of sufficient quantity and quality to counteract the negative losses of the prior three years. In fact, as discussed below, during the Relevant Period, the Individual Defendants determined that Popular U.S.'s goodwill was impaired for the same reasons it should have established a valuation reserve for its deferred tax assets. The

Individual Directors had direct evidence that there was not sufficient income to carry the Company's goodwill, but inexplicably they failed to carry over that conclusion to the Company's reasoning with respect to Popular U.S.'s deferred tax asset valuation allowance.

92. Defendant PwC, Popular's auditor, observed in its 2007 "Guide to Accounting for Income Taxes" that a projection of future income is insufficient to avoid a valuation allowance when a corporation has cumulative losses in recent years:

> A projection of future taxable income is inherently subjective and generally will not be sufficient to overcome negative evidence that includes cumulative losses in recent years, particularly if the projected future taxable income is dependent on an anticipated turnaround to operating profitability that has not yet been demonstrated.[1]

4. SFAS 109 and Tax Planning Strategies

93. In determining the amount of a valuation allowance when faced with significant negative evidence such as a cumulative three-year loss and/or rapidly deteriorating results and business prospects, an enterprise can take into account "tax planning strategies." SFAS 109, ¶ 22. However, SFAS 109 provides that tax planning strategies must meet stringent standards to legitimately avoid recognition of a valuation allowance. The strategies must be actions that: "(a) are prudent and feasible, (b) an enterprise ordinarily might not take, but would take to prevent an operating loss or tax credit carryforward from expiring unused, and (c) would result in realization of deferred tax assets." *Id*.

94. Auditor Defendant PwC has stated in its own tax guide that "[m]oving income from a nontax jurisdiction to a taxable one solely to realize net operating loss carryforwards" is an "Action[] That Generally Would Not Qualify as Tax-Planning Strategies" to avoid a valuation allowance under SFAS 109. ("Guide To Accounting for Income Taxes" at 117.)

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[1] PwC "Guide to Accounting for Income Taxes" at 93 (2007) available at http://www.pwc.com/us/en/insurance/accounting-for-income-taxes-guide-2007.jhtml.

95. Also, the "[i]mplementation of the tax-planning strategy must be primarily within the control of management" for it to meet the "prudent and feasible" requirements of GAAP. SFAS 109, ¶ 107. As the Company admitted within months of announcing that it was relying on tax strategies to carry its deferred tax assets, the strategies were fundamentally flawed and the Company was required to establish a full valuation allowance in the fourth quarter of 2008.

F. Individual Defendants Breached Their Fiduciary Duties By Allowing Popular to Implement a Deferred Tax Asset Strategy that Violated GAAP – SFAS 109

96. Throughout the Relevant Period, Individual Defendants maintained that Popular's consolidated financial statements are prepared in accordance with GAAP, including SFAS 109. As detailed herein, however, Individual Defendants allowed and/caused the Company to violate GAAP by failing to record a valuation allowance for Popular U.S.'s deferred tax assets. This failure was caused by Individual Defendants recklessly disregarding multiple "red flags" that amounted to substantial negative evidence about Popular U.S.'s ability to generate future taxable income to realize its deferred tax assets. The negative evidence ignored by Individual Defendants throughout the Relevant Period included: (i) Popular U.S.'s operations were sold off and significantly downsized, further constraining its ability to produce taxable income in the future; (ii) Popular U.S. was experiencing rapidly declining income since 2005; (iii) Popular U.S. sustained a cumulative loss for the three years ending at each and every quarter beginning December 31, 2007 and continuing through December 31, 2008; (iv) Popular U.S. suffered increasing loan losses as the financial and housing markets began their high-profile collapses; and (v) Popular was forced to seek additional capital on behalf of Popular U.S. through TARP and a public offering of preferred stock.

97. Despite these red flags, Individual Defendants also failed to acknowledge the impact of these red flags on the Company's ability to produce future taxable income or otherwise provide any positive evidence that would be sufficient to overcome the significant amount of negative evidence requiring a valuation allowance to be recorded for Popular U.S.'s deferred tax asset.

98. Furthermore, the Company's proposed "tax strategies" did not meet the "prudent and feasible" GAAP requirements, as Popular itself recognized shortly after announcing the purported strategies.

1. Individual Defendants Knew that Downsizing Popular U.S. Would Make It "More Likely than Not" that the U.S. Operations Could Not Produce Future Taxable Income to Realize the Benefits of Its Deferred Tax Assets

99. The Individual Defendants should have started to record a valuation allowance to reduce Popular U.S.'s deferred tax assets in the Company's Form 10-K for the year ended December 31, 2006, filed on March 1, 2007. The valuation allowance should have been recorded then because, as early as January 9, 2007 (well before the filing date), the Individual Defendants knew, or were reckless in not knowing and/or were grossly negligent, that it was "more likely than not" that Popular U.S. would not be capable of producing the future taxable income necessary to realize a benefit from its deferred tax assets, as required under GAAP. However, the Individual Defendants allowed and/or caused the Company to record Popular U.S. deferred tax assets without taking any valuation allowance for 18 months after the March 11, 2007 filing. The Individual Defendants waited until October 22, 2008 to take only a partial valuation allowance.

100. Indeed, on January 9, 2007, the beginning of the Relevant Period, Individual Defendants announced that PFH was exiting the wholesale subprime mortgage origination business, resulting in charges of $39 million. Specifically, Popular announced that the "management," including Individual Defendants, had adopted a PFH Restructuring Plan, which called for PFH to exit the wholesale subprime mortgage loan origination business during early first quarter of 2007 and to shut down the wholesale broker, retail and call center business divisions. The Individual Defendants' PFH Restructuring Plan also called for the consolidation of PFH support functions with its sister U.S. banking entity, Banco Popular North America, creating a single integrated North American financial services unit.

101. The need to restructure or sell PFH was known to the Individual Defendants even earlier than January 2007. Upon information and belief and based upon the allegations contained within the Consolidated Class Action Complaint filed in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG

(D.P.R.), CW2, a former Senior Vice President, Chief Risk Officer and Credit Officer at PFH from June 2005 through December 2008, who reported directly to Popular's CEO and Board of Directors, stated that Popular realized that Popular U.S.'s subsidiary, PFH, was not profitable in the Fall of 2005 and thus decided to downsize or sell PFH. CW2 stated that in November 2005, Popular retained the consulting firm Speer & Associates to "come in and sort of help dissect the organizations profitability and that's when they came up with the game plan to lay people off and close down certain businesses and keep a couple of other businesses open." Popular then began to implement this plan in early 2006.

102. Similarly, CW3, a Senior Financial Analyst and accountant at PFH from July 2004 through July 2007, was responsible for compiling income statement summaries, also referred to as profitability reports for each subsidiary under PFH, including Equity One. CW3 confirmed that there had been a "pretty consistent decline in profitability" at PFH and that PFH was "not making any money" from at least as early as August 2004. CW3 described PFH as a "sinking ship from beginning to end" throughout CW3's tenure at the Company. CW3 also stated that the subprime business was "a very large part" of PFH, and that when it started to fall apart prior to 2007, it "certainly put a hurting" on the Company. In addition, CW3 stated that "the Company [all business segments and divisions under the PFH umbrella] was not in a good situation from beginning to end."

103. CW4, an Operations Analyst at Equity One from August 2005 through March 2008, also confirmed that Popular U.S.'s senior management "knew that certain entities under PFH were struggling" as early as August 2005 when CW4 started at the Company. CW4 confirmed that the loan losses were increasing throughout CW4's tenure at Equity One. According to CW4, the Company had several layoffs to mask these losses, which meant, however, that there were not as many employees to pay attention to collecting on delinquencies.

104. Despite this negative evidence that the Individual Defendants were aware of, or recklessly disregarded, the Individual Defendants did not provide any positive evidence to justify not recording a valuation allowance in its March 11, 2007 Form 10-K.

105. The PFH Restructuring Plan was just the beginning of the Individual Defendants' plan to divest Popular from its U.S. operations. Throughout the remainder of 2007 and the beginning of 2008, Popular significantly downsized its other U.S. operations through either sales or restructurings that burdened Popular with additional losses and greatly reduced the possibility that Popular U.S.'s remaining operations could produce the future taxable income necessary to realize the benefits of its deferred tax asset.

106. On November 9, 2007, the Individual Defendants allowed and/or caused Popular to file its Form 10-Q for the third quarter of 2007, in which it announced that the Individual Defendants had adopted a Restructuring Plan for Popular U.S.'s internet financial services subsidiary E-LOAN. Popular announced that:

> Considering the losses in the operation of E-LOAN, market conditions and other factors, the Board of Directors approved a substantial reduction of marketing and personnel costs at E-LOAN. This change will include concentrating marketing investment toward the internet and the origination of first mortgage loans that are actually being sold to Government Sponsored Entities ("GSEs").

107. The Individual Defendants' E-LOAN Restructuring Plan called for substantially reducing the size of E-LOAN, and would "result in the elimination of approximately 513 positions out of a total of 771 and will be substantially accomplished in the fourth quarter of 2007." Popular acknowledged that "this change in E-LOAN's business model could result in impairment in the value of its recorded goodwill and trademark," of up to $164.4 million and $47.3 million, respectively, further demonstrating the deteriorating potential for future taxable income in the U.S.

108. SFAS 142, Goodwill and Intangible Assets, was issued in June 2001. It governs the accounting for goodwill and establishes rules for how frequently the GAAP carrying value of goodwill must be reevaluated and the conditions that require a write-down of goodwill, as the Individual Defendants did here in 2007. Goodwill is the result of purchasing another entity for more than the fair value of the target entity's assets minus the fair value of its liabilities. The excess price paid is frequently attributed to extra value created by a unique product, position in the marketplace, superior management, or another competitive advantage. This competitive advantage is expected to

generate superior profits. However, marketplaces change, management turns over and the financial markets can deteriorate and those paid for future profits can vanish.

109. SFAS 142 requires that when the expectation of those future profits disappears, the goodwill associated with those future profits must be written off. SFAS 142, ¶ 18 requires that the evaluation of goodwill be done at a "reporting unit" level. SFAS 142, ¶ 28 further requires the evaluation (fair value testing) of goodwill to be done "annually or more frequently if conditions warrant." In 2007, the Individual Defendants wrote off Popular's goodwill related to its U.S. operations. Footnote 12 to the Company's 2007 annual report, describes the Company's reasoning and methodology used to conclude that a write-off of goodwill was required. It stated:

> The amount included in the other category related mostly to impairment losses of \$164,410,000 in the Banco Popular North American reportable segment that were associated with the write-off of E-LOAN's as a result of E-LOAN's Restructuring Plan described in Note 2 to the consolidated financial statements. In determining the fair value of a reporting unit, the Corporation generally uses a combination methods, including … discounted cash flow analysis

110. In order for the Individual Defendants to have reached a conclusion that the goodwill associated with Popular U.S. was impaired by use of the discounted cash flow analysis they must have examined future cash flows. These cash flows are, by definition, derived from projections of future profits or losses. These are the same projections for the same reporting unit that would be used to assess the likelihood of future taxable income from which to recover the Company's deferred tax assets. It is implausible, if not impossible, to conclude that the same expectations of future profits on one hand cannot justify carrying E-LOAN's goodwill, while on the other hand justify carrying the Company's deferred tax asset. This is particularly egregious given the Company's deferred tax asset was four times as large as E-LOAN's goodwill, which was fully written-off. According to its 2007 annual report, the Company's consolidated gross deferred tax asset was \$602 million and the E-LOAN goodwill asset was \$164 million.

111. Even if the Company still had any goodwill related to its banking operations in the U.S.; it was clearly a violation of GAAP and a breach of the Individual Defendants' fiduciary duties because none of the deferred tax assets associated with its E-LOAN operation were written-off.

Further, given the concerns about U.S. profitability evidenced by the Individual Defendants' evaluation of whether the Company's U.S. goodwill was recoverable, it follows that the Individual Defendants, and particularly Defendant Junquera , the Audit Committee and its financial experts, and the Company's auditor, Defendant PwC, had in hand the information necessary to evaluate the recoverability of Popular U.S.'s deferred tax asset. However, they all recklessly disregarded this negative evidence.

112. Despite the fact that the Individual Defendants announced the E-LOAN Restructuring Plan, which, in addition to their PFH Restructuring Plan, would significantly diminish Popular U.S. ability to produce taxable income, in its Form 10-Q, the Individual Defendants failed to record any valuation allowance to offset Popular U.S.'s deferred tax assets in the very same Form 10-Q. In light of this negative evidence, the Individual Defendants did not provide any positive evidence to justify not recording a valuation allowance.

113. The Individual Defendants knew about the problems at E-LOAN earlier than November 2007. CW5 was the Vice President of Finance at E-LOAN throughout the Relevant Period until April 2009. CW5, who reported to both the President of E-LOAN and the CFO of BPNA, stated that prior to the start of 2008 "it was pretty evident that there would be a slowdown in business at E-LOAN." In fact, CW5 stated that there was "concern and discussions amongst management at the Company about a decrease in the business as a whole" by that time. As a result, according to CW5, by the beginning of 2008, the Company had started forecasting a decrease in volume. CW5 also stated that due to the Company's expectation of decreased business, Popular began planning for a reduction in force as early as September 2007, which it ultimately implemented in November 2007. CW5 also confirmed that BPNA worked closely with Popular PR to determine the deferred tax assets to be recorded. CW5 said that the final figure was provided to the BPNA tax department by Popular's tax department.

114. Similarly, CW6, an Assistant Vice President in Business Banking from January 2006 through June 2008 in charge of business development, stated that E-LOAN was "never profitable" while under BPNA. CW6 said that BPNA was a good company until E-LOAN was acquired, which

was known for its poor quality loans. According to CW6, once E-LOAN was acquired, BPNA began approving more questionable loans, including some that had already been rejected by E-LOAN. Though CW6 was provided with the underwriting guidelines, the loans being approved did not meet the underwriting guidelines. CW6 also stated that despite the poor quality of loans, the Company did not have any policies or practices in place to handle loans delinquencies. CW6 and other employees complained about the quality of loans being approved and were mistreated and then fired (which is why CW6 and others filed a wrongful termination class action against the Company which was eventually settled). Indeed, CW6 recounted a meeting in Chicago in October 2007 – more than three months before the beginning of the Relevant Period – when "things were getting really bad," at which the CEO of BPNA, Individual Defendant Herencia, told CW6 and other business bankers that the Company was in "struggling times" and that the Company was seeing negative effects on some of the businesses it purchased.

115. A week after Popular announced the Individual Defendants' E-LOAN Restructuring Plan, Moody's placed Popular's ratings on review for "possible downgrade." Moody's review was based on its opinion that "the ongoing credit market disruption will make it more challenging for Popular to finance its Popular Financial Holdings consumer loan subsidiary. That subsidiary is the source of most of Popular's U.S. subprime mortgage portfolio and has been financed largely with short- and medium-term wholesale borrowings. A particular challenge for Popular is that the turmoil in credit markets has been marked by an aversion on the part of investors to finance any subprime-related assets." This should have served as another warning to the Individual Defendants that Popular U.S. would not likely produce future taxable income.

116. On December 21, 2007, the Individual Defendants allowed and/or caused Popular to announce further developments aimed at eliminating the PFH subprime lending business and effectuate the E-LOAN restructuring. First, Popular had recharacterized \$3.2 billion of on-balance sheet securitizations as "sales" under GAAP which had the effect of removing approximately \$2.4 billion in subprime loans from its books. Because Popular was so desperate to get these subprime loans off its books, however, it had to take a loss. The Individual Defendants estimated at that time

that it would need to take a net loss of "approximately $90 million and $165 million" as a result of recharacterizing these loans. Second, as a result of the Individual Defendants' E-LOAN Restructuring Plan, it would have to recognize goodwill and intangible impairment charges of $164.4 million and $47.3 million, respectively.

117. On this news, Moody's promptly downgraded Popular's credit rating. Moody's concluded that "[r]esidual interests, in the form of IOs and MSRs, will remain on Popular's balance sheet, as will an additional $2.7 billion of subprime mortgages. The remaining U.S. subprime exposure, combined with the impairment of the E-LOAN platform and the lackluster profitability of Popular's U.S. branch banking business, highlight significant challenges in Popular's U.S. operations that will take time to resolve."

118. In downgrading Popular's credit rating, Moody's specifically relied upon Popular's liquidity problems and the inability of Popular to make a profit through its U.S. operations. Moody's reported that "Popular's holding company liquidity needs over the next twelve months remain significant. Specifically, the Popular North America holding company balance sheet at September 2007 noted more than $1 billion in debt maturing within one year at that point in time, in addition to the commercial paper then outstanding." Further, Moody's stated that "2008 will be challenging from a profitability standpoint. Popular's core Puerto Rico market is expected by many economic observers to remain in a recession, ***the [U.S.] economy is also expected to be under pressure and Popular's subprime exposures will likely require elevated provisioning***." (Emphasis added.)

119. Similarly, securities analyst firm Sterne Agee reported on January 15, 2008 that its "main concern with Popular remains credit which continues to deteriorate driven by continued recessionary trends in Puerto Rico coupled with continued weakness in U.S. markets."

120. On January 23, 2008, the Individual Defendants allowed and/or caused the Company to announce that management had agreed to sell a significant portion of the mortgage loan and consumer finance portfolio of Equity One, the consumer finance operation of PFH, to American

121. After the sale of PFH's Equity One, all that remained of Popular U.S.'s operations were the substantially reduced E-LOAN business, BPNA, and the remnants of PFH, consisting of roughly $1.2 million of loan and mortgage servicing assets and a very small manufactured housing loan portfolio.

122. Despite the massive, year-long downsizing of Popular U.S.'s operations from January 2007 to January 2008, and the subsequent negative analyst reports discussed above, the Individual Defendants failed to record any valuation allowance to offset Popular U.S.'s growing deferred tax assets in any of its SEC filings, including the Company's Form 10-K for fiscal year 2007 filed on February 29, 2008. In that year, the Individual Defendants allowed and/or caused Popular U.S.'s gross deferred tax assets to grow from $360 million at the end of 2005 to $437 million at the end of 2006 to $602 million at the end of 2007, a $165 million, or 37%, increase. Despite significant growth of the deferred tax assets and the negative evidence surrounding Popular U.S.'s shrinking operations, the Individual Defendants failed to provide any positive evidence to justify not recording a valuation allowance during these periods.

123. On August 29, 2008, the Individual Defendants allowed and/or caused the Company to announce that it was selling approximately $1.2 billion of loans and mortgaging servicing assets of PFH to various Goldman Sachs affiliates. Although the transaction would provide Popular with $700 million in liquidity and reduce Popular's subprime exposure, it would also impose on Popular an additional significant loss of $450 million, further limiting any likelihood of future taxable income from Popular U.S.'s operations. That taxable income was needed to realize its deferred tax assets.

124. On September 11, 2008, *Business News Americas* reported that Popular hired Citigroup to find a buyer for BPNA. Given that the Individual Defendants were considering selling the U.S. operations, and since Popular had been absorbing losses on its recent sales, it continued to

be "more likely than not" that Popular U.S. could not have expected to recognize future taxable income to offset Popular's roughly $800 million U.S. gross deferred tax asset as of September 2008.

125. On September 18, 2008, the Individual Defendants allowed and/or caused the Company to announce the sale of PFH's manufactured housing loan assets at a $70 million pre-tax loss to 21st Mortgage Corp. & Vanderbilt Mortgage and Finance.

126. The Individual Defendants' willingness to incur significant ongoing losses to restructure E-LOAN and PFH, and sell PFH's $1.2 million remaining loan portfolio and manufactured housing loan assets, demonstrates that the Individual Defendants recognized from the beginning of the Relevant Period that losses from Popular U.S.'s operations were an ongoing condition. These ongoing losses left the Individual Defendants, including PwC, with no basis to conclude it was "more likely than not" that Popular U.S. would be able to realize the benefit of its deferred tax assets as required by GAAP.

127. Moreover, the significant negative evidence that Popular was unlikely to realize the benefit of its U.S. deferred tax assets continued to mount throughout the Relevant Period. The consistent and cumulative losses at Popular U.S., as discussed below, demonstrate that Popular needed to take a valuation allowance on all of its U.S. mainland deferred tax assets by the beginning of the Relevant Period inescapable.

128. Indeed, Popular U.S. had reported significant pre-tax losses for four of the five quarters ending December 31, 2007, with pre-tax losses over that period of roughly $669 million. Similarly, Popular U.S.'s PFH unit had operated at a loss for ten consecutive quarters ending that same period, and Popular planned to impose additional losses on PFH through its PFH Restructuring Plan. Likewise, Popular U.S.'s E-LOAN business segment had operated at a significant loss for each of the four quarters ending at December 31, 2007, and Popular's E-LOAN Restructuring Plan had so severely damaged E-LOAN's brand that Popular had to recognize a major goodwill and trademark impairment charge of $211.8 million. Finally, Popular U.S.'s commercial and retail banking operation, BPNA, began to operate at a significant loss by the fourth quarter of 2006, which

except for a *de minimis* profit of $1.6 million in the second quarter of 2007, continued unabated through December 31, 2008 and the Company's most recent quarter September 30, 2009.

129. Nevertheless, when faced with these consistent U.S. losses in its major U.S. operating segments, the Individual Defendants continued to recognize the full value of the Company's U.S. deferred tax assets on its books for at least 18 months after announcing the Individual Defendants' first PFH Restructuring Plan in January 2007. This was the case even after the Individual Defendants approved the write-off of goodwill and intangible assets in 2006 (related to PFH) and 2007 (related to E-LOAN) as a result of determining there was insufficient future income to justify carrying those assets at any value. Tellingly, the Individual Defendants failed to acknowledge that future income for goodwill impairment testing and future income for deferred tax asset valuation allowance did not exist. Notably, using this same underlying test under GAAP, the Individual Defendants lacked any valid justification for failing to establish a valuation allowance.

130. When the Individual Defendants did decide to record a partial valuation allowance in the Company's third quarter Form 10-Q, filed on November 10, 2008, they did so only because the Individual Defendants claimed that Popular U.S. had just experienced a three-year cumulative loss. As discussed herein, the three-year cumulative loss was actually realized nine months earlier. Additionally, given the precipitous decline in pretax income from 2005 forward, a valuation allowance should have been recognized as early as December 31, 2006. Indeed, the Individual Defendants never mentioned that the greatly diminished Popular U.S. operations played a role in their decision to record a partial valuation allowance. The Individual Defendants, however, recognized Popular U.S.'s ongoing poor performance for its third quarter net loss of $668.5 million. In fact in the October 22, 2008 press release announcing the loss, the Individual Defendants attributed "the decision announced two months ago to sell the assets and discontinue the operations of PFH" for the huge loss.

131. At all relevant times, the Individual Defendants knew or recklessly disregarded that Popular U.S. did not retain sufficient operations capable of producing future taxable income to realize its deferred tax assets. In particular:

- The Individual Defendants repeatedly acknowledged prior to and during the Relevant Period that Popular U.S. had been performing poorly and was expected to continue to do so in 2008 and 2009 due to the U.S. financial crisis;

- The Individual Defendants personally issued each and every one of the adverse press release announcements and SEC disclosures cited above;

- The Individual Defendants reviewed and certified the accuracy of Popular's financial statements, including Popular's 2006 10-K filed on March 1, 2007, Form 10-Q for the third quarter of 2007 filed November 7, 2007, the January 24, 2008 report of its earnings and 2007 10-K filed on February 29, 2008, which reported Popular U.S.'s earnings for 2005-2007, and revealed that Popular U.S. was operating at a three-year cumulative loss as of December 31, 2007;

- Defendant Junquera had intimate knowledge regarding Popular U.S.'s poor performance due to his intimate familiarity with Popular's U.S. operations. As B. Riley reported on September 18, 2007, Defendant Junquera had supervised Popular's original expansion efforts into the mainland United States between 1996-2001; and

- The Individual Defendants knew the significant negative impact recording valuation allowance for Popular U.S.'s deferred tax assets in Popular's financial statements would have on the Company's core business areas. If the Individual Defendants allowed a full valuation allowance to be recorded, it would demonstrate that Popular U.S. was not "well-capitalized." Under FDIC regulations, if Popular was deemed to be undercapitalized it would have been prohibited from engaging in core operations, including non-banking activities and brokered deposit activities.

2. Since 2005, Popular U.S. Reported a Precipitous Decline in Pre-Tax Income and Worsening Losses Culminating in a Three-Year Cumulative Loss Which Defendants Failed to Overcome with Positive Evidence as Required by GAAP

132. In March 2007, a little over two months after the Company first announced the Individual Defendants' plan to downsize Popular U.S.'s PFH business; the Individual Defendants announced that Popular U.S. had experienced a $161 million drop in pre-tax income between fiscal year 2005 and fiscal year 2006. Despite this additional negative evidence, the Individual Defendants failed to record a valuation allowance in the same Form 10-K that announced the massive $161 million drop in-pre tax income as required by GAAP. Moreover, the following year, the Individual

Defendants announced a staggering $645 million loss for Popular U.S. This represented a three-year cumulative loss, which as SFAS 109, ¶103, states, "is a significant piece of negative evidence that is difficult to overcome." Yet, the Individual Defendants once again violated GAAP by failing to provide any positive evidence that would demonstrate that it was "more likely than not" that Popular U.S.'s deferred tax assets would be realized and that Popular did not need to record a valuation allowance.

133. Specifically, on March 15, 2006, the Individual Defendants allowed, and/or caused Popular to file, the Company's Form 10-K for the year ending December 31, 2005. Popular reported an estimated $171 million of pre-tax income for 2005 for its Popular U.S. operations.

134. On March 11, 2007, the Individual Defendants allowed, and/or caused Popular to file, the Company's Form 10-K for the ending December 31, 2006. Popular reported an estimated $10 million pre-tax income for 2006 for its Popular U.S. operations. This represented a $161 million deterioration of pre-tax income from 2005, a 94% drop in pre-tax income from 2005 to 2006. The Individual Defendants recognized in the Company's 2007 Proxy Statement, filed on March 15, 2007, that PFH's net income for 2006 failed to surpass the Company's pre-established minimum thresholds.

135. On February 29, 2008, the Individual Defendants allowed, and/or caused Popular to file, the Company's Form 10-K for the year ending December 31, 2007. Popular reported an estimated $(645) million pre-tax loss for 2007 for its Popular U.S. operations. This represented a decline of $655 million of pre-tax income from 2006 to 2007, and an $816 million difference in net pre-tax income between 2005 and 2007. In the Company's 2008 Proxy Statement, filed on March 12, 2008, the Individual Defendants allowed and/or caused the Company to state:

> 2007 was a very difficult year for the [Company's] business in the United States, Popular North America, Inc., and ***its results of operations for 2007 was considerably below the pre-established threshold***. This was mainly due to losses suffered as a result of extremely difficult mortgage and credit markets, Popular Financial Holdings, Inc. restructuring plans and loan recharacterization transaction and the restructuring plan at E-LOAN, Inc. which led to goodwill and trademark impairments. Popular North America's financial difficulties had a significant impact

> on the Corporation's results of operations. The [Company] experienced a 2007 net loss of approximately $64.5 million and, therefore, did not reach the minimum performance threshold of approximately $344 million of net profit.

(Emphasis added.)

136. Based on the reported Popular U.S. pre-tax income above at ¶¶ 132-135, for the years ended December 31, 2005 and December 31, 2007, Popular U.S. was at a three-year cumulative loss position, with a cumulative pre-tax loss of $(465) million, as demonstrated in the chart below:

	2005	**2006**	**2007**
Pre-Tax Income (Loss)	$171M	$10M	$(645M)
Yearly Decline	n/a	$(161)M	$(655M)
Cumulative Loss			**$(465M)**

137. Indeed, Popular realized cumulative loss for the three years 2005, 2006 and 2007 on December 31, 2007; well before September 30, 2008, as the Individual Defendants first claimed in the Company's November 10, 2008 Form 10-Q. In the third quarter 2008 Form 10-Q, the Individual Defendants wrongly state:

> The Corporation's U.S. mainland operations are in a cumulative loss position for the three-year period ***ended September 30, 2008***. For purposes of assessing the realizibility of the deferred tax assets in the U.S. mainland, this cumulative loss position is considered significant negative evidence and has caused us to conclude that the Corporation will not be able to fully realize the deferred tax assets in the future.

(Emphasis added.)

138. Although the Individual Defendants recognized that the Company had experienced a three-year cumulative loss, as detailed above, they were at least nine months late in recognizing the cumulative loss and recording a valuation allowance. Thus, pursuant to SFAS 109, since the Individual Defendants failed to provide any positive evidence to overcome this "significant piece of negative evidence," the Individual Defendants were required to record a valuation allowance in the Company's 2007 Form 10-K filed on February 29, 2008, not November 10, 2008.

a. The Individual Defendants' Justifications for Failing to Declare a Full Valuation Were Unsupportable and Violated GAAP

1. Individual Defendants' Reliance on the 20-Year Expiration Term to Justify Not Recording a Full Valuation Allowance

139. Instead of recording a valuation allowance in the Company's 2007 Form 10-K filed on February 29, 2008, the Individual Defendants reported Popular U.S.'s full deferred tax assets without providing any information or positive evidence to overcome the "significant" and "difficult to overcome" negative evidence of the three-year cumulative loss in Popular U.S. Indeed, the Individual Defendants provided the following disclosure about Popular U.S.'s ability to realize its deferred tax assets:

> The only portion of the deferred tax asset that has a limited life is the portion related to the net operating loss carryforward of the Corporation's U.S. operations. Since its expiration term is of 20 years, the Corporation expects to generate enough taxable income prior to such expiration term to fully realize it. ***Based on the information available as of March 31, 2008, the Corporation expects to fully realize the net deferred tax asset.***

(Emphasis added.)

140. The Individual Defendants relied on the same language, updated for the time period, in Popular's Form 10-Q for the first quarter of 2008, filed on May 12, 2008 and the Company's Form 10- Q for the second quarter of 2008, filed on August 11, 2008.

141. The Individual Defendants' reliance on a standard 20-year expiration term for Popular U.S.'s deferred tax assets was an improper and insufficient basis to avoid a valuation allowance under SFAS 109. As detailed above, SFAS 109, ¶ 20 requires that an enterprise look to "[i]nformation about an enterprise's current financial position and its results of operations for current and preceding years." Further, financial information should be "supplemented by all currently available information about future years." *Id*.

142. The standard 20-year expiration term explanation of Popular U.S.'s deferred tax assets, does not explain whether Popular U.S. would be "more likely than not" to earn future taxable income to realize the benefit of the deferred tax assets as is required under GAAP. The standard 20-year expiration term simply provides no evidence about whether Popular U.S. itself would be able to

generate sufficient net income to realize the benefit of those tax assets as is required under GAAP. That was particularly true given that Popular U.S. had been operating at a cumulative three-year loss since December 31, 2007 and had been experiencing steadily deteriorating pre-tax income since 2005.

143. As SFAS 109, ¶103 explains, the FASB's view that a deferred tax asset be more likely than not to be realized "requires positive evidence of sufficient quality and quantity to counteract negative evidence in order to support a conclusion that, based on the weight of all available evidence, a valuation allowance is not needed." Because the Individual Defendants' standard 20-year expiration term justification did not provide any positive financial evidence of Company-specific future income from Popular U.S. to offset its deferred tax assets, it was plainly insufficient to justify avoiding a valuation allowance in both the first and second quarters of 2008.

144. Moreover, PwC, Popular's auditor, has recognized that it would have been improper under GAAP for the Individual Defendants to rely upon undisclosed forecasts of future profits to avoid a valuation allowance in the face of its cumulative three-year loss and steadily decreasing income:

> A projection of future taxable income is inherently subjective and generally will not be sufficient to overcome negative evidence that includes cumulative losses in recent years, particularly if the projected future taxable income is dependent on an anticipated turnaround to operating profitability that has not yet been demonstrated.[2]

145. PwC, however, failed to follow its own guidelines and allowed Popular to continue to avoid recording a valuation allowance based on unsupportable justifications that violated GAAP.

2. Individual Defendants' Reliance on Unsupportable "Tax Strategies" Did Not Justify Failing to Record a Full Valuation Allowance

146. Two months after proclaiming that the standard 20-year expiration of Popular's U.S. deferred tax assets justified not taking a full valuation allowance, Popular belatedly conceded on

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2 PwC, "Guide to Accounting for Income Taxes" at 93 (2007).

October 22, 2008 that due to its three-year cumulative loss position it was required to record a valuation allowance against Popular U.S.'s deferred tax assets. Notwithstanding the fact that the Company actually realized a three-year cumulative loss nine months earlier, the Individual Defendants, instead of recording a full valuation allowance as they should have done at the beginning of the Relevant Period, only recorded a partial valuation allowance, which did not cover $323 million in U.S. mainland deferred tax assets. In an attempt to justify their failure to record a full valuation allowance, the Individual Defendants in Popular's Form 10-Q filed on November 10, 2008, claimed that a full allowance was not necessary because of two new purported "tax strategies." The Individual Defendants, however, failed to provide any substantive detail about those tax strategies. In fact, prior to this announcement, Popular had not previously disclosed that it was applying any tax strategy whatsoever that impacted the U.S. deferred tax assets.

147. In the Form 10-Q filed on November 11, 2008, the Individual Defendants stated:

> In assessing the realizability of the deferred tax assets, management has considered all four sources of taxable income mentioned above, including its forecast of future taxable income, which includes assumptions about the unprecedented deterioration in the economy and in credit quality. The forecast includes costs reductions initiated in connection with the reorganization of the U.S. mainland operations and two tax planning strategies. The two strategies considered in management's analysis include the level of interest expense in the U.S. by transferring debt to the Puerto Rico operations and the transfer of a profitable line of business to the U.S. mainland operations.

148. Importantly, the Individual Defendants failed to include: (1) what debt Popular would attempt to transfer from Popular U.S. to Popular PR; (2) how Popular would transfer such debt; (3) what the transfer of debt would cost; and (4) what the effect of the transfer of debt would have on the Company financially. Similarly absent from this announcement is: (1) what profitable business line Popular would attempt to transfer from Puerto Rico to Popular U.S.; (2) how Popular would transfer this business line; (3) what the transfer of the business line would cost; and (4) what the effect of the transfer of the business line would have on the Company financially.

149. The Individual Defendants' reliance on these two new purported tax strategies was also an improper method of avoiding tax valuation allowances under GAAP. As Popular's auditor, PwC stated in its own tax guide, "[m]oving income from a nontax jurisdiction to a taxable one solely to realize net operating loss carryforwards" is an "Action[] That Generally Would Not Qualify as Tax-Planning Strateg[y]" to avoid a valuation allowance under SFAS 109. PwC, "Guide To Accounting for Income Taxes" at 117.

150. Moreover, since these purported tax planning strategies required the consent of third-party regulators, including Puerto Rican bank regulators whose job is to protect the solvency of the country's financial institutions, these strategies could not been deemed "primarily within the control of management" and, therefore, "feasible" for GAAP planning purposes. SFAS 109, ¶107.

151. Specifically, because Popular is a highly regulated organization, it would face significant scrutiny from, among others, the FDIC, the I.R.S., the Federal Reserve, and the Office of Comptroller of Currency and the Office of the Commissioner of Finance and Insurance of Puerto Rico, about the viability and legitimacy of such transfers, particularly during the banking crisis occurring in the Fall of 2008. For example, Popular would need to first obtain the consent of the Puerto Rico tax authorities to move a profitable line of business to Popular U.S. The requirement of obtaining such regulatory consent alone would make this tax planning strategy no longer primarily in the control of management," as required to be valid under SFAS 109. *Id*. Indeed, the Individual Defendants admitted that they generally did not have such control in Popular's filings with the SEC. For example, Popular stated in its 2007 Form 10-K that "[p]ositions taken in the Corporation's tax returns may be subject to challenge by the taxing authorities upon examination."

152. Furthermore, the Individual Defendants' intent to only move Popular PR's profits and not the actual business from this "profitable line of business" to Popular U.S. would have been hard-pressed to receive the approval of the cash-strapped Puerto Rican government. Conversely, in the event that the Individual Defendants intended to move both Popular PR's business and profits to Popular U.S., Popular would have needed to expend considerable cash it did not have available because it was undercapitalized. Accordingly, the Individual Defendants breached their fiduciary

duties by proposing these tax planning strategies that were an improper basis to avoid a full valuation allowance under GAAP.

153. Even if the Individual Defendants' tax planning strategies were within management's control – which they were not – Popular also did not have a line of business in Puerto Rico that was profitable enough to absorb the remaining $323 million in Popular U.S. deferred tax assets and simultaneously not threaten the viability of Popular PR's operations.

154. Since at least 2006, the Puerto Rican economy had been in a recession. Accordingly, at the beginning of the Relevant Period in 2008, Puerto Rico had already been in a recession for over 2 years – the longest recession to ever hit Puerto Rico – and numerous economic observers and analysts projected that the recession would continue unabated for a number of years. Specifically, economic observers and analysts were forecasting a continued significant contraction in Puerto Rico's economy for 2008 and unemployment rates exceeding 11%. Consumer sentiment indices in Puerto Rico also forecasted a long-term economic slump; more than 65% of consumers expected the economy in Puerto Rico to get worse over the course of the year.

155. Puerto Rico's economy only worsened over the course of the Relevant Period. Economic observers and analysts noted that the local economy remained under heavy pressure via higher oil prices, and that there were no signs of positive economic catalysts in either the near or distant future.

156. The Individual Defendants were well aware of the impact the recession in Puerto Rico had on the Company's ability to earn revenue. For example, in the Company's Form 10-K for the year ended December 31, 2007, the Company stated:

> A significant portion of the Corporation's financial activities and credit exposure is concentrated in Puerto Rico (the "Island") and the Island's economy has been deteriorating.

157. The Individual Defendants also knew or recklessly disregarded that the Puerto Rico recession would continue to have a significant negative impact on Popular's ability to generate revenue in 2008 and 2009. For example, in a September 3, 2008 Form 8-K which attached a June

30, 2008 investor presentation entitled "Kaufman Bros.," Popular stated that "Management expects weakness in the [Puerto Rico] economy to continue throughout 2008 and into 2009."

158. Then, in a November 18, 2008 Form 8-K which attached a B. Riley investor presentation, Popular stated "the challenging P.R. [Puerto Rico] economy is pressuring profitability at the segment. The ongoing recession and deteriorating quality trends in the commercial and construction loan portfolios, have led to an increase in credit costs. Management expects weakness in economy to continue into 2009."

159. Given the impact of the Puerto Rico recession on Popular's financial statements, Popular simply could not afford to transfer a hugely profitable business from Puerto Rico to the mainland U.S. in order to benefit from the remaining U.S. deferred tax assets.

160. Indeed, upon information and belief and based upon the allegations contained within the Consolidated Class Action Complaint filed in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG (D.P.R.), CW1, a Vice President and Regional Manager at BPNA from November 2003 to November 2008, responsible for running BPNA's problem loan and workout area for New York and Florida, stated that he did not believe there were any profitable businesses in Puerto Rico in 2008 that could have been successfully transferred to Popular U.S. In fact, CW1 observed that at the end of 2008, "the Puerto Rican market was even weaker than the U.S. market."

161. All of these facts reveal that the purported tax planning strategies relied upon by the Individual Defendants to avoid taking a full valuation allowance were an improper attempt to continue to avoid recording a full valuation. Given the Individual Defendants' decision to sell off assets and significantly downsize Popular U.S., as well as Popular U.S.'s history of mounting loan losses, the Individual Defendants could not properly avoid material tax valuation allowances on the Company's large and growing U.S. deferred tax assets throughout the Relevant Period. Indeed, as discussed herein, these purported tax planning strategies were completely infeasible and accordingly abandoned just two months later when the Individual Defendants decided to "confront reality."

162. At all relevant times, the Individual Defendants knew or recklessly disregarded that Popular's reliance on purported "tax strategies" to avoid recording a full valuation allowance against Popular's U.S. mainland deferred tax assets violated GAAP. In particular:

- The Individual Defendants repeatedly demonstrated their knowledge of the relevant GAAP requirements by quoting SFAS 109 in the Company's Forms 10-K and 10-Q throughout the Relevant Period, and repeatedly claiming that the Company's financial statements complied with SFAS 109. SFAS 109 is unambiguous that tax strategies must be "prudent," "feasible" and within "management's control" to avoid taking a valuation allowance;

- Before the Company's 2008 third quarter Form 10-Q, the Individual Defendants never disclosed reliance on any purported "tax planning strategies" and never disclosed any of the specific risks associated with those strategies. Even thereafter, when the purported tax planning strategies were introduced, the Individual Defendants failed to offer any specifics supporting the strategies as required by GAAP;

- The Individual Defendants knew or recklessly disregarded that Popular's purported tax strategies required regulatory approval, and therefore were not in the control of management, in violation of GAAP;

- The Individual Defendants knew or recklessly disregarded that Popular's purported tax strategies were extremely costly and risky to the Company; and

- The Individual Defendants knew or recklessly disregarded that the transfer of a profitable line of business from Puerto Rico was not feasible or prudent because Popular PR's operations were being significantly and negatively impacted by the Puerto Rico recession. Given the Company's severe liquidity crisis, transferring a business to the U.S. from Puerto Rico would have been improper and far too expensive for the Company to implement.

3. Individual Defendants Failed to Provide Any Positive Evidence that Popular U.S.'s Losses Were "Temporary" and Due to "Unprecedented Market Conditions"

163. Having "confronted reality," the Individual Defendants abandoned their tax strategies justification and provided yet another reason for its failure to write down the deferred tax assets by January 2007 in the Company's 2008 Form 10-K filed on March 2, 2009. Specifically, the Individual Defendants maintained that the Company did not need to take a valuation allowance for all of its U.S. deferred tax assets at that time because Popular U.S.'s cumulative taxable loss was "temporary" and due to "unprecedented market conditions."

164. However, Popular U.S.'s cumulative three-year pre-tax loss which began in the fourth quarter of 2007 was far from temporary. Popular U.S. has suffered losses ranging from $24 million to $473 million in seven of the eight quarters ending September 30, 2008, with the second quarter of 2007 being the outlier with a *de minimis* pre-tax profit of $1.6 million.

165. Indeed, CW1 stated that after Popular U.S. sustained its loss in 2007, CW1 "did not hear or see anything within the company that indicated that Popular had any chance whatsoever of booking a profit in 2008." In fact, CW1 stressed that there was nothing to indicate that things at the company "were going to turn around." According to CW1, Popular knew that the Company was going to take a larger loss in 2008 than in 2007, "and it did."

166. CW7, a Senior Financial Analyst for BPNA from August 2007 until December 2008, confirmed that that the financial statements reflected the North American subsidiaries were constantly losing money throughout CW7's tenure, which CW7 believed was mostly due to the amount of subprime loans. In fact, according to CW7, the Company stopped seeking new business and was merely "running the [existing] portfolio." This does not indicate that the continuous losses Popular U.S. was experiencing were going to be "temporary" as the Individual Defendants maintained.

167. The Individual Defendants' reliance on "unprecedented current market conditions" to explain why they did not feel the need to write-down Popular U.S's. deferred tax assets by March 1, 2007 was also unsupportable. For more than a year before it finally recorded a full valuation allowance of Popular U.S.'s deferred tax assets, the Individual Defendants had been blaming "unprecedented" market conditions for Popular U.S.'s skyrocketing losses. For example, in an October 19, 2007 press release explaining the significant losses for Popular U.S., Popular stated that its U.S. operations had trouble maintaining liquidity and earnings because "[t]he U.S. credit markets have been marked by unprecedented instability and disruption since the beginning of the third quarter of 2007."

168. Furthermore, the Individual Defendants knew that the financial crisis would have a long-term effect on Popular, and Popular U.S. in particular. In their publicly filed statements, Individual Defendants even explicitly addressed the financial crisis and its effect on the Company:

- Weakness in the economy and in the real estate market in the geographic footprint of Popular has adversely impacted and may continue to adversely impact Popular. 2007 Form 10-K, filed on February 29, 2008.

- The current state of the economy and uncertainty in the private and public sectors has had an adverse effect on the credit quality of the Corporation's loan portfolios. The continuation of the economic slowdown could cause those adverse effects to continue, as delinquency rates may increase in the short-term, until more sustainable growth resumes. Also, a potential reduction in consumer spending may also impact growth in other interest and non interest revenue sources of the Corporation. *Id.*

- A prolonged economic slowdown, a continuing decline in the real estate market in the U.S. mainland, and ongoing disruptions in the capital markets have harmed and could continue to harm the results of operations of PFH, one of the Corporation's business segments. *Id.*

- The housing market in the U.S. is undergoing a correction of historic proportions. After a period of several years of booming housing markets, fueled by liberal credit conditions and rapidly rising property values, since early 2007, the sector has been in the midst of a substantial dislocation, since 2007. It has had a significant impact on some of the Corporation's U.S-based business sectors and has the potential to affect its ongoing financial results and condition. Declining property values could impact the credit quality of the Corporation's U.S. mortgage loan portfolio because the value of the homes underlying the loans is a primary source of repayment in the event of foreclosure. *Id.*

169. Indeed, Defendant Junquera later acknowledged how bad Popular U.S. was doing in 2007 and 2008 at a March 4, 2009 Keefe, Bruyette & Woods Regional Bank Conference following the end of the Class Period:

- "When we look at our US operations here it was a problem as we cited and where we are losing a lot of money. Our biggest problem was the acquisition business of subprime asset through Popular Financial Holdings like (inaudiable) in the US. And it took us a couple of years to clean up the balance sheet here. And finally we have sold the assets of that company but it came at a price. We did have to take huge losses that were reflected in 2007 and—principally in 2008."

- Our experiences here in the US mainland, although we were able to grow assets, we were not able to grow them in a very profitable way. We were making money marginally during normal time. And now during difficult times, you know we're losing money. So we have changed the platform. And now it will be operated as a region of Puerto Rico."

- "Liquidity . . . It was a very serious problem from the end of '07 throughout '08."

170. Despite recognizing the potential impact of the financial crisis, despite the ongoing and increasing and cumulative losses suffered by Popular U.S., Defendant Junquera acknowledged that he and the Individual Defendants ignored this mountain of negative evidence and continued to inflate the Company's earnings by failing to record a valuation allowance and violating GAAP.

b. The Individual Defendants Knew the Company Was Required to Take a Full Valuation Under GAAP

171. At all relevant times, the Individual Defendants knew or recklessly disregarded that Popular U.S. was in a cumulative loss position and was continuing to experience quarter after quarter of decreasing pre-tax income by the start of the Relevant Period because:

- The Individual Defendants repeatedly acknowledged prior to and during the Relevant Period that Popular U.S. had been performing poorly and was expected to continue to do so in 2008 and 2009 due to the U.S. financial crisis;

- The Individual Defendants reviewed and certified the accuracy of Popular's financial statements, including Popular's 2006 10-K filed on March 1, 2007, Form 10-Q for the third quarter of 2007 filed November 7, 2007, the January 24, 2008 report of its earnings and 2007 10-K filed on February 29, 2008, which reported Popular U.S.'s earnings for 2005-2007, and revealed that Popular U.S. was operating at a three-year cumulative loss as of December 31, 2007;

- The Individual Defendants, and in particular Defendant Junquera, who has an extensive financial background, and members of the Audit Committee, including its financial experts, Director Defendants Salerno and Teuber, knew or recklessly disregarded the significant negative evidence created by Popular U.S.'s three-year cumulative loss and ongoing decreasing pre-tax losses. SFAS 109 is unambiguous that such a loss is significant negative evidence that is difficult to overcome;

- The Individual Defendants repeatedly demonstrated their knowledge of SFAS 109 by quoting it in the Company's Forms 10-K and 10-Q throughout the Relevant Period, and by repeatedly claiming that the Company's financial statements complied with SFAS 109; and

- The magnitude and the duration of the cumulative pre-tax losses and overstated deferred tax assets could not have been lost on the Individual Defendants, who misstated the value of Popular U.S.'s deferred tax assets by hundreds of millions of dollars for nearly two years; and

- The Individual Defendants knew the significant negative impact recording valuation allowance for Popular U.S.'s deferred tax assets in Popular's financial statements would have on the Company's core business areas. If the Individual Defendants allowed a full valuation allowance to be recorded it would demonstrate that Popular U.S. was not "well-capitalized." Under FDIC regulations, if Popular was deemed to be undercapitalized, it would have been prohibited from engaging in core operations, including non-banking activities and brokered deposit activities;

3. Rising U.S. Mortgage Defaults Increased Popular's Loan Loss Reserves Making it Even More Unlikely Than Not that Popular U.S. Would Realize Its Deferred Tax Assets

172. As a result of the fallout of the U.S. subprime mortgage industry collapse in late 2006 and the ensuing financial crisis, Popular incurred a considerable increase in loan losses. As demonstrated in the chart below, in 2005, Popular's provision for loan losses was only $195,272,000. But by 2006, the Individual Defendants grew Popular's provision for loan losses by 50% to $287,800,000 and by 2007 it had doubled to $562,700,000:

Year	Loan Loss	% Increase From Prior Year
2004	$178.6M	n/a
2005	$195.2M	9%
2006	$287.8M	47%
2007	$562.6M	96%

173. As the Company's loan loss reserves increased, Popular U.S.'s construction portfolios continued to deteriorate as the quality of its U.S. mortgages decreases and the number of non-performing loans continued to increase. The increase in its loan loss reserve and the ongoing

deterioration of its U.S. loan portfolios were clear examples that Popular U.S. had no realistic prospects for earning future taxable income by which it could realize its deferred tax asset. These problems were expected to continue and still continue for Popular U.S. However, the Individual Defendants ignored these high-profile problems and failed to record any valuation allowance until November 2008, over a year and half after the collapse of the subprime market and a year after the financial crisis hit the United States.

174. The chart below details the amount of deferred tax assets the Individual Defendants recorded for each quarter beginning with the third quarter of 2006. In addition to providing the deferred tax assets recorded, the chart also provides the change in recorded deferred tax assets, quarter by quarter, as well as the valuation allowance recorded during each quarter and what percentage of gross deferred tax assets that allowance represented. Importantly, the chart provides the negative evidence, discussed above, that the Individual Defendants knew or should have known at the time of the Company's filing.

2006

Quarter Date Filed	**Q3 2006 11/9/06**	**Q4 2006 3/1/07**
Recorded Deferred Tax Assets ("DTA")[3]	$306M	$437M
Quarterly DTA Change	(18.8%)	42.8%
Valuation Allowance	($39,000)	($39,000)
Valuation Allowance - % of DTA Known Negative Evidence Concerning Popular U.S. at the Time of Filing	0.01% - PFH and E-Loan operating at a loss	0.01% - Downsizing Popular U.S. PFH Restructuring Plan announced - PFH and E-LOAN operate at a loss - PFH records million goodwill impairment charge - 47% increase in loan loss reserves - U.S. subprime mortgage market begins to collapse and mortgage defaults begin to rise

[3] Popular did not record gross deferred tax assets for the following quarters Q1 2006, Q2 2006, Q3 2006, Q1 2007, and Q2 2007. As a result, the DTAs for those quarters in these charts are "net" deferred tax assets, meaning that gross deferred tax assets are reduced by gross deferred tax liabilities for those quarters.

2007

Quarter Date Filed	Q1 2007 5/10/07	Q2 2007 8/9/07	Q3 2007 11/9/07	Q4 2007 2/29/08
Recorded DTA	$358M	$420M	$420M	$602M
Quarterly DTA Change	(18.1)%	17.3%	0.0%	43.3%
Valuation Allowance	($39,000)	($39,000)	($39,000)	($39,000)
Valuation Allowance - % of DTA	0.01%	0.01%	0.01%	0.01%
Known Negative Evidence Concerning Popular U.S. at the Time of Filing	- Downsizing Popular U.S. PFH Restructuring Plan continues - PFH and E-LOAN continue to operate at a loss - Increasing loan loss reserves - U.S. subprime market collapsed and mortgage defaults continue to rise	-Downsizing Popular U.S. PFH Restructuring Plan continues - Increasing loan loss reserves - U.S. housing market collapsed and mortgage defaults continue to rise	- Downsizing Popular U.S. -PFH Restructuring Plan continues -E-LOAN Restructuring Plan announced - E-LOAN records $228 million goodwill impairment charge -Popular U.S. experiencing pre-income tax loses - Increasing loan loss reserves - U.S. housing markets collapsed and mortgage defaults continue to rise - Moody's downgraded Popular	- Popular U.S. at a three-year cumulative loss position - Downsizing Popular U.S. -PFH and E-LOAN Restructuring Plans continue - Popular U.S. experiencing pre-income tax loses - 96% increase in loan loss reserves - U.S. financial crisis begins - U.S. housing markets collapsed and mortgage defaults continue to rise - Moody's downgraded Popular

2008

Quarter Date Filed	Q1 2008 5/12/08	Q2 2008 8/11/08	Q3 2008 11/10/08	Q4 2008 3/2/09
Recorded DTA	$694M	$808M	$1.024B	$1.351B
Quarterly DTA Change	15.2%	16.4%	26.7%	31.9%
Valuation Allowance	($39,000)	($39,000)	($360.4M)	($860M)
Valuation Allowance - % of DTA	0.01%	0.01%	35.2%	63.7%
Known Negative Evidence Concerning Popular U.S. at the Time of Filing	-Popular U.S. continues to be at a three-year cumulative loss position -Downsizing Popular U.S. -PFH and E-LOAN Restructuring Plans continue -Sale of Equity One assets announced -Popular U.S. continues to experience pre-income tax loses -High loan loss reserves -U.S. financial crisis continues -U.S. housing markets collapsed	-Popular U.S. continues to be at a three-year cumulative loss position -Downsizing Popular U.S. -PFH, Equity One and E-LOAN Restructuring Plans continue -Popular U.S. continues to experience pre-income tax loses -High loan loss reserves -U.S. financial crisis continues -U.S. housing markets collapsed	-Popular U.S. continues to be at a three-year cumulative loss position -Downsizing Popular U.S. -PFH, Equity One and E-LOAN Restructuring Plans continue -Sale of PFH assets announced -Individual Defendants shopping BPNA for a sale -Popular U.S. continues to experience pre-income tax loses High loan loss reserves -U.S. financial crisis continues -U.S. housing markets collapsed	-Popular U.S. continues to be at a three-year cumulative loss position -Popular U.S. significantly downsized -Popular U.S. experiencing pre-income tax loses -Participating in TARP -High loan loss reserves -U.S. financial crisis continues -U.S. housing markets collapsed

4. Failure to Record Valuation Allowance Inflated Earnings and Allowed the Individual Defendants to Avoid FDIC Sanctions

175. As demonstrated above, the Individual Defendants failed to record an appropriate valuation allowance against Popular U.S.'s deferred tax assets in violation of GAAP throughout the Relevant Period despite the considerable amount of negative evidence that is difficult to overcome. By failing to record proper quarterly valuation allowances, the Individual Defendants not only inflated reported earnings and capital in violation of GAAP and in breach of their fiduciary duties, but were also able to avoid potentially crippling-FDIC sanctions by maintaining the appearance of a "well-capitalized" bank.

176. Since at least January 9, 2007, the Individual Defendants knew, or recklessly disregarded the fact, that Popular U.S. would be unable to realize its deferred tax assets because the Individual Defendants were significantly downsizing Popular U.S. due to increasing losses, poor business prospects and unsustainable housing and financial markets. Nevertheless, the Individual Defendants reported full deferred tax assets without recording any meaningful valuation allowance against them. This artificially inflated the Company's earnings and capitalization.

177. The Individual Defendants' failure to comply with GAAP became more conspicuous as they reported higher and higher deferred tax assets. Since the fourth quarter of 2006, the Individual Defendants allowed and/or caused Popular to nearly triple its reported gross deferred tax assets from $437 million to $1.3 billion, a nearly billion dollar change.

178. As Popular acknowledged in its public filings, virtually all of the increase in its deferred tax assets during the Relevant Period were derived from losses at Popular U.S. Indeed, by the end of the Relevant Period, when Popular finally recorded the appropriate valuation allowance on its U.S. mainland deferred tax assets, the portion of Popular's gross deferred tax assets from Popular U.S. had grown to $861 million, all of which required a valuation allowance reducing the GAAP carrying value of Popular's U.S. deferred tax asset to zero.

179. The Individual Defendants' failure to record the appropriate valuation allowance and reduce Popular U.S.'s deferred tax assets prior to December 31, 2008 artificially inflated Popular's reported earnings and capital every quarter accumulating to hundreds of millions of dollars by December 31, 2008. Further, the Individual Defendants' improper accounting for Popular U.S.'s deferred tax assets artificially inflated its liquidity, making Popular U.S. appear to have more earnings and capital than it actually had. In particular, the Individual Defendants used the improperly reported Popular U.S.'s deferred tax assets to conceal the fact that, as of the second quarter of 2008, Popular U.S. was no longer "well-capitalized" under the regulations promulgated under the Federal Deposit Insurance Act ("FDIA"). Had this fact been disclosed, it would have had dramatic consequences for Popular's stock price, and would have prevented Popular from operating

as a financial holding company permitted to engage in key non-banking activities under the Gramm-Leach-Bliley Act and from holding or earning interest on brokered deposits.

180. Indeed, by the second quarter of 2008, analysts and rating agencies were constantly concerned about, and commenting on, Popular's deteriorating liquidity. For example, on May 13, 2008, Moody's changed its rating outlook on Popular to "negative" from "stable." Moody's reported that this change "reflects Moody's concerns regarding Popular's weakening. . . liquidity profile." In particular, Moody's noted that Popular's usual liquidity sources "have been constrained by Popular's recent earnings challenges in its U.S. business."

181. In response to those concerns, the Individual Defendants were forced to resort to desperate measures to preserve capital and improve liquidity. First, on May 22, 2008, as further discussed below, the Individual Defendants allowed and/or caused the Company to announce the Offering of $400 million of Series B preferred stock. The Individual Defendants made clear at the time that the proceeds of the preferred stock offering would be used for purposes including "increasing Popular's liquidity and capital."

182. Then, on August 28, 2008, the Individual Defendants allowed and/or caused the Company to announce that it would cut its quarterly dividend to investors in half, from $0.16 to $0.08, saving the Company $90 million in capital per year. In connection with this announcement, Defendant Carrión stated that "this is absolutely a necessary step given the continued uncertainty in the financial markets and extended fallout of the U.S. housing sector. . . . [t]he new rate will provide us with greater flexibility by significantly increasing our liquidity."

183. Furthermore, as discussed above, by late-August 2008, Popular's liquidity situation had become so dire that the Individual Defendants had to resort to selling off the remaining U.S. operation assets at significant losses.

184. The Individual Defendants' desperate need for an infusion of capital was confirmed by former employees of the Company. For example, upon information and belief and based upon the allegations contained within the Consolidated Class Action Complaint filed in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG (D.P.R.), CW8, a District Manager for Equity One from February 2007

through March 2008, stated that Equity One was sold to help Popular survive. CW8 explained that CW8 was told on conference calls by the President of Equity One, Bill Williams, and the Executive Vice President of Equity One, Mike Duganich, that Popular used the funds from the sale of Equity One to give a "cash infusion to keep Banco Popular propped up while we weather the storm."

185. CW9, an Operations Manager for PFH/Equity One from early 2002 through early 2008, also confirmed that the sale of Equity One was done because parts of the business were not profitable.

186. Ultimately, the Individual Defendants' need for liquidity grew so urgent that they actively sought to sell virtually the remainder of Popular U.S.'s operations. On September 11, 2008, *Business News Americas* reported that Popular had hired Citigroup to find a buyer for BPNA. This was due to the Individual Defendants' pressure to boost liquidity levels to repay $880 million in debt coming due in the second quarter of 2009.

187. In fact, the Individual Defendants' liquidity situation became so bad that in November 2008, they were forced to petition the U.S. government on behalf of Popular for a significant amount of funding from TARP. On November 18, 2008, Popular obtained preliminary approval from the government to access $950 million in TARP funds through the Capital Purchase Program. This transaction closed on December 5, 2008.

188. Notably, Defendant Junquera admitted in a March 4, 2009 conference, that "[l]iquidity. . . It was a very serious problem from the end of '07 throughout '08."

189. The capital shortage which was the cause of Popular's liquidity crisis, similarly affected the status of Popular's regulatory capital. Accordingly, the Individual Defendants were highly motivated not to record a valuation allowance for the U.S. mainland deferred tax assets.

190. Indeed, had the Individual Defendants recorded a valuation allowance for Popular U.S.'s deferred tax assets as they were required to do under GAAP, Popular U.S.'s total risk-based capital ratio would have fallen below the 10% FDIA regulatory threshold for being "well-capitalized" beginning in the second quarter of 2008. This would have left Popular U.S. merely "adequately capitalized" in both the second and third quarters of 2008.

191. Had the Individual Defendants not engaged in the $400 million Series B Offering and received the $950 million in TARP funds on behalf of Popular in December 2008 and recorded a valuation allowance for Popular U.S.'s deferred tax assets as they were required to do under GAAP, both Popular U.S.'s and Popular PR's total-risk based capital ratio would have fallen below 8%, falling from "well-capitalized" to a catastrophic "undercapitalized" in the fourth quarter of 2008.

192. The difference between being classified by the FDIA as "well-capitalized" as opposed to be classified as either "adequately capitalized" or "undercapitalized" was material to Popular and its shareholders, and would have had immediate and significant repercussions on the Individual Defendants' ability to conduct business and earn income on behalf of the Company.

193. As the Individual Defendants described in Popular's 2007 Form 10-K, the FDIA establishes five capital tiers: "well-capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," and "critically undercapitalized." The relevant capital measures are the total risk-based capital ratio, the tier 1 risk-based capital ratio and the leverage ratio.

194. Rules adopted by the federal banking agencies provide that a depository institution will be deemed to be: (1) "well-capitalized" if it maintains a leverage ratio of at least 5%, a tier 1 risk-based capital ratio of at least 6% and a total risk-based capital ratio of at least 10% and is not subject to any written agreement or directive to meet a specific capital level; (2) "adequately capitalized," if it is not "well-capitalized," but maintains a leverage ratio of at least 4% (or at least 3% if given the highest regulatory rating in its most recent report of examination and not experiencing or anticipating significant growth), a tier 1 risk-based capital ratio of at least 4% and a total risk-based capital ratio of at least 8%; (3) "undercapitalized" if it fails to meet the standards for adequately capitalized institutions (unless it is deemed significantly or critically undercapitalized); (4) "significantly undercapitalized" if it has a leverage ratio of less than 3%, a tier 1 risk-based capital ratio of less than 3% or a total risk-based capital ratio of less than 6%; and (5) "critically undercapitalized" if it has tangible equity equal to 2% or less of total assets.

195. To calculate a corporation's total risk-based capital ratio and tier 1 capital ratios under FDIA requirements, the corporation's capital is stated as a ratio in comparison to its total assets or a

risk-weighted basis according to its credit risk. tier 1 capital includes shareholder equity, retained earnings and deferred tax assets. Tier 2 capital consists of other types of capital, such as undisclosed reserves, revaluation reserves, general provisions, hybrid instruments and subordinated term debt. The remainder of a corporation's assets not included in tier 1 and tier 2 capital includes riskier assets, such as subprime debt. A corporation's total risk-based capital ratio is derived by taking the sum of its tier 1 and tier 2 capital, and dividing it by all of the corporation's assets weighted by credit risk.

196. Throughout the Relevant Period, the Individual Defendants reported that Popular was "well-capitalized." However, had the Individual Defendants acted in accordance with GAAP and recorded a valuation allowance for Popular U.S.'s deferred tax assets, Popular U.S. would have fallen from "well-capitalized" to just "adequately capitalized" beginning in the second quarter of 2008.

197. In addition, if the Individual Defendants had not been bailed out by the U.S. government by receiving $950 million in TARP funds during the fourth quarter of 2008, Popular U.S.'s total risk-based capital ratio would have fallen to a catastrophically low 7.32%. That would have left Popular U.S. "undercapitalized" under FDIA requirements. Similarly, Popular PR would have fallen to a virtually identical ratio.

198. On September 23, 2008, an analyst at Sterne Agee specifically put Popular on notice of this problem when it warned that Popular was "undercapitalized." Sterne Agee noted that Popular's $450 million loss on the PFH sale to Goldman plus a required "DTA valuation allowance that could be anywhere from $200-$400 million or more and a sale of U.S. assets that could trigger additional losses (including goodwill) in excess of $500 million, we remain concerned as to capital levels."

199. Had the Individual Defendants reported that, in reality, Popular was not "well-capitalized," it would have suffered material and catastrophic repercussions. Most significantly, under the requirements of the Gramm-Leach-Bliley Act, Popular's failure to maintain a "well-capitalized" rating, would mean that it could not remain a financial holding company permitted to

engage in a wide range of nonbanking activities. As a result, the Individual Defendants would have been forced to shut down or spinoff a number of its businesses, including at a minimum, PFH, Popular Insurance, Inc., Puerto Rico Popular Life REIT, Popular Insurance V.I., Popular Financial Management LLC, Popular Securities, Inc. and E-LOAN Insurance Services.

200. Further, had the Individual Defendants correctly reported that it was not in fact "well-capitalized," Popular would have been restricted from continuing to hold approximately $3 billion in brokered deposits on its financial statements and from receiving the customary higher interest on such brokered deposits, without a waiver from the FDIC. Brokered deposits are investment vehicles similar to Certificates of Deposit ("CDs"), but instead involve an FDIC broker accumulating a large amount of money (usually through multiple investors) and then providing that pool of money to the bank. Investors find brokered deposits attractive because banks usually offer a larger return than for traditional CDs – usually more than 75 basis points over the prevailing market rate – in exchange for this larger influx of capital. Brokered deposits are restricted for banks that are not "well-capitalized" to prevent a bank from using them to support unsound or rapid expansion of its loan or investment portfolio, and from destabilizing interest rates in its market.

201. The Individual Defendants acknowledged in Popular's 2007 Form 10-K that FDIC restrictions would have barred the Company from retaining any brokered deposits without an FDIC waiver, and would have barred Popular from paying attractive interest rates if Popular U.S. was not well-capitalized:

> **Brokered Deposits**
>
> FDIC regulations adopted under FDIA govern the receipt of brokered deposits. Under these regulations, a bank cannot accept, roll over or renew brokered deposits unless it is (i) well-capitalized or (ii) adequately capitalized and receives a waiver from the FDIC. A bank that is adequately capitalized may not pay an interest rate on any brokered deposits, and a bank that is undercapitalized may not pay an interest rate on any deposits, in excess of 75 basis points over certain prevailing market rates specified by regulation. There are no such restrictions on a bank that is well-capitalized. The Corporation does not believe the brokered deposits regulation has had or will have a material effect on the funding or liquidity of Banco Popular and BPNA.

202. The Individual Defendants further admitted that Popular principally relied on brokered deposits to maintain its liquidity during the Relevant Period:

> Brokered deposits, which amounted to $3.1 billion at December 31, 2008, continued to be used as an important funding source of on-hand liquidity amidst the financial industry developments in the second half of 2008. The level of brokered deposits at year-end 2008 was at the same level as in the previous year. ***One of the strategies followed by management during 2007 in response to the unprecedented market disruptions was the utilization of brokered deposits to replace short-term uncommitted lines of credit***.

(Emphasis added.)

203. Thus, had the Individual Defendants disclosed the truth about Popular U.S. not being "well-capitalized," that would have threatened an important source of $3.1 billion in liquidity. Popular also would have lost the ability to attract future brokered deposits with attractive interest rates. This would also have had a significant impact on Popular's earnings, as it would not have been able to accrue the significant amount of interest income it derived from such brokered deposits.

204. Finally, had the Individual Defendants disclosed that Popular U.S. was no longer "well-capitalized," they would have caused rating agencies and analysts to significantly downgrade their ratings of Popular's debt and investment recommendations for Popular's stock.

205. In short, the potentially catastrophic consequences of the Individual Defendants disclosing that Popular U.S. was not "well-capitalized" beginning in the second quarter of 2008 gave the Individual Defendants a significant motive to breach their fiduciary duties to the Company and its shareholders and fail to record proper valuation allowances on Popular U.S.'s deferred tax assets.

206. At all relevant times, the Individual Defendants knew or recklessly disregarded that Popular's improper accounting artificially inflated the Company's reported earnings, liquidity and regulatory capital ratios. In particular:

- The Individual Defendants repeatedly demonstrated their knowledge of the relevant FDIC requirements for being "well-capitalized" by quoting the FDIC and Gramm-Leach- Bliley Act requirements extensively in Popular's SEC filings and by repeatedly claiming that the Company was well-capitalized under those regulatory requirements;

- The Individual Defendants certified Popular's financial statements disclosing Popular's regulatory capital ratios using numbers that improperly included Popular U.S.'s deferred tax assets that Popular U.S. was more likely than not to be unable to realize;

- The Individual Defendants knew the tremendous impact the FDIC and Gramm-Leach-Bliley Act "well-capitalized" requirements had on Popular's ability to earn revenue from essential non-banking activities and carry and earn interest from approximately $3 billion of brokered deposits;

- Given the severe repercussions from failing to be "well-capitalized," the Individual Defendants knew or recklessly disregarded that disclosing a material tax valuation allowance would threaten the Company's ability to qualify as "well-capitalized" under FDIA regulations;

- Beginning in the Summer of 2008, Sterne Agee questioned repeatedly whether Popular was undercapitalized and stated in September 2008 that the "Company Remains Undercapitalized." The Individual Defendants did not respond; and

- The Individual Defendants repeatedly acknowledged that Popular was experiencing significant liquidity issues in its U.S. operations due to the economic crisis in the U.S., but failed to discuss how that impacted the Company's capitalization ratio.

5. The Individual Defendants Finally Record a Full Valuation Allowance

207. Finally, on January 22, 2009, the Individual Defendants finally revealed the need to record a full valuation allowance for Popular U.S.'s deferred tax assets. The Individual Defendants caused Popular to issue a press release announcing its financial results for the fourth quarter and year ending December 31, 2008 for the period ended December 31, 2008. For the quarter, the Individual Defendants reported a net loss of $702.9 million for Popular and highlighted as a "principal item" that "impacted" its results a "valuation allowance on the Corporation's deferred tax assets related to the U.S. operations of $462.8 million."

208. The Individual Defendants again cited the U.S. operations' cumulative loss position as the basis for its valuation allowance. They stated that "this cumulative loss position, along with evaluation of all sources of taxable income available to realized the deferred tax asset . . . is considered significant negative evidence and has caused management to conclude that the

> [Popular's] substantial loss for the fourth quarter [was] principally caused by a significant increase in the allowance for loan losses and ***the valuation allowance equal to 100% of the deferred tax asset related to [its] U.S. mainland operations***" and that the "provision for loan losses increased particularly in the construction sector in Puerto Rico and in the U.S. mainland and the mortgage related loans in [Popular's] U.S. mainland portfolios.

(Emphasis added.)

209. Addressing the specific factors requiring that Popular finally recognize such a large loss, the Individual Defendants emphasized, among other things, the Company's previously undisclosed credit loss understatements, understated (and under-reserved) loan loss provisions, unreported asset impairments, overstated deferred tax assets related to Popular U.S.'s operations, declining yields in the Company's loan and investment portfolios, higher loan net charge-offs, understated (and under-reserved) specific reserves for commercial, construction and mortgage loans, and the fact that "home equity lines of credit and second lien mortgage loans" Popular issued were "behaving as unsecured loans due to devaluation in [the] real estate" market, stating in relevant part that:

> The following principal items impacted the Corporation's continuing operations financial results for the quarter ended December 31, 2008, when compared to the same quarter in the previous year:
>
> - ***higher provision for loan losses by $267.1 million as a result of higher credit losses and increased specific reserves for impaired loans;***
> - ***valuation allowance on the Corporation's deferred tax assets related to the U.S. operations of $462.8 million recorded during the fourth quarter of 2008****; and*
>
> * * *
>
> - Net income for the Banco Popular de Puerto Rico ("BPPR") reportable segment for the quarter ended December 31, 2008 amounted to $12.4 million, compared to $80.2 million in the same quarter of the previous year. ***The financial results were principally impacted by an increase in the provision for loan losses of $112.7 million primarily related to the commercial and construction loan portfolios. During the fourth quarter of 2008, several commercial and construction loans in the BPPR reportable segment reported further deterioration due to current economic conditions requiring their classification as impaired loans under SFAS No. 114 or an increase in their specific reserves. As of December 31, 2008, there were $639 million of SFAS No. 114 impaired loans in the BPPR reportable segment with a***

BPPR's reportable segment net interest income for the fourth quarter of 2008 declined $13.8 million, compared to the same quarter in the previous year. ***This decrease was principally related to lower volume of investment securities and to lower yields in the loan and investment portfolios,*** partially offset by lower cost of funds. Despite the impact of the unprecedented market conditions and historical reductions in interest rates by the Federal Reserve ("FED"), the BPPR reportable segment maintained a healthy net interest margin that approximated 3.89% for the quarter ended December 31, 2008, compared to 3.91% in the same quarter of the previous year. Non-interest income increased for the quarter by $10.4 million, or 8%, principally in other service fees and service charges on deposits accounts. Operating expenses in this reportable segment decreased by $3.4 million when comparing quarterly periods. This decline was partly the result of successful control management efforts and reduced compensation tied to financial performance.

Banco Popular North America ("BPNA") reportable segment reported net losses of $349.5 million for the quarter ended December 31, 2008, compared to net losses of $218.3 million in the fourth quarter of 2007. ***The quarterly financial results were principally impacted by an increase in the provision for loan losses of $156.4 million. The increase in the provision for loan losses considered higher loan net charge-offs, specific reserves for commercial, construction and mortgage loans, as well as the impact of the deterioration in the U.S. residential housing market that has also affected home equity lines of credit and second lien mortgage loans which are behaving as unsecured loans due to devaluation in real estate.*** This reportable segment also recognized a valuation allowance on deferred tax assets of $200.1 million during the fourth quarter of 2008. These unfavorable variances were in part offset by the reduction in impairment losses on intangible assets of E-LOAN which was previously described.

During the quarter ended December 31, 2008, the BPNA reportable segment recorded approximately $33.8 million in charges such as severance costs, lease cancellations, and write-downs of intangibles and long-lived assets that were associated to the restructuring plans of its banking operations and E-LOAN. As indicated in the Form 10-Q filed on November 10, 2008, in October 2008, the Corporation's ***Board*** of Directors approved a restructuring plan for BPNA with the objective of reducing the size of its banking operations in the U.S. mainland to a level suited to present economic conditions, improve profitability in the short term, increase liquidity and lower credit costs and, over time, achieve a greater integration with corporate functions in Puerto Rico. Also, the Board of Directors approved a plan for E-LOAN to cease operating as a direct lender effective in the fourth quarter of 2008. Refer to the Corporation's Form 10-Q for the quarter ended September 30, 2008 for further information.

The integration of both banking subsidiaries, BPPR and BPNA, under one management ***continues*** to be implemented, as part of the previously announced restructuring plan for the U.S. operations. The business divisions of retail banking and commercial banking, in addition to administrative and operational personnel, at Banco Popular North America, are now reporting to management in Puerto Rico.

Losses of $75.2 million, net of tax, related to the discontinued operations of Popular Financial Holdings ("PFH") in the U.S. mainland for the fourth quarter of 2008. The net losses for the ***quarter*** ended December 31, 2008 corresponding to the discontinued operations included $37.8 million in valuation allowances on the Corporation's deferred tax assets. Also, the net loss included non-interest losses of $24.3 million for the quarter ended December 31, 2008 consisting of additional write-downs in loans accounted at fair value as of year end and the final impact of the sale of assets to Goldman Sachs announced in the third quarter of 2008 and that closed in November 2008. Operating expenses for the discontinued operations amounted to $34.1 million for the fourth quarter of 2008, which primarily included charges related to the final settlement on the sale to Goldman Sachs, personnel costs and other restructuring charges related to the discontinuance of the operations. As of December 31, 2008, PFH holds only $13 million in assets, of which $7 million are loans measured at fair value.

Net Loss from Continuing Operations - Fourth Quarter 2008 compared to Fourth Quarter 2007:

* * *

Net Interest Income

Net interest income for the fourth quarter of 2008 was $288.9 million, compared with $337.3 million for the fourth quarter of 2007. The decrease was due to a decline of $1.3 billion in average earning assets, together with a reduction of 40 basis points in the net interest margin.

* * *

The decline in average earning assets was due mostly to the runoff of investment securities as part of a strategy of deleveraging the balance sheet. The reduction in the average balance of investment securities was used to repay short-term borrowings, including repurchase agreements. In the loan portfolio, an increase in average commercial loans outstanding was offset in part by declines in mortgage and auto loans.

The decline in the net interest yield was driven by a reduction in the yield of earning assets. This was caused primarily by the decline in the yield of commercial loans, which have a significant amount of floating rate loans whose yield decreased as the Fed cut the funds rate in 2008. The Fed lowered the federal funds target rate between 400 and 425 basis points from December 31, 2007 to December 31, 2008. Also contributing to the reduction in the yield of commercial loans is the substantial increase in non-performing loans as described later in this press release. The Corporation's average cost of funds decreased driven by a reduction in the cost of deposits and short-term borrowings.

Offsetting partially the decline in the cost of deposits and short-term borrowings was an increase in the cost of long-term borrowings. During 2008, certain medium-term notes matured which had been issued in previous years at relatively low rates were some replaced with more expensive term funds whose cost reflects the current distressed conditions of the credit markets. Also contributing to the reduction in the net interest yield was the net loss for the year which reduced available funds obtained through capital.

Provision for Loan Losses and Credit Quality

The provision for loan losses in the continuing operations totaled $388.8 million, or 174% of net charge-offs, for the quarter ended December 31, 2008, compared with $121.7 million or 157%, respectively, for the same quarter in 2007, and $252.2 million, or 148%, respectively, for the quarter ended September 30, 2008. The provision for loan losses for the quarter ended December 31, 2008, when compared with the same quarter in 2007, reflects higher net charge-offs by $146.2 million, mainly in construction loans by $63.0 million, consumer loans by $28.8 million, commercial loans by $37.0 million, and mortgage loans by $15.1 million. Provision and net charge-off information for prior periods was retrospectively adjusted to exclude discontinued operations for comparative purposes.

The higher level of provision for the quarter ended December 31, 2008 was mainly attributable to the continuing deterioration in the commercial and construction loan portfolios due to current economic conditions in Puerto Rico and the U.S. mainland. Credit deterioration trends in the Corporation's commercial loan portfolio are reflected across all industry sectors. The allowance for loan losses for commercial and construction credits has increased, particularly the specific reserves for loans considered impaired. Also, deteriorating economic conditions in the U.S. mainland housing market have impacted the mortgage industry delinquency rates. The Corporation has recorded a higher provision for loan losses in the fourth quarter of 2008 to cover for inherent losses in the mortgage portfolio of the Corporation's U.S. mainland operations as a result of higher delinquencies and net charge-offs, and consideration of troubled debt restructurings in the mortgage portfolio, principally from the non-conventional business of Banco Popular North America. Furthermore, consumer loans net charge-offs rose principally due to higher losses on home equity lines of credit and second lien mortgage loans of the Corporation's U.S. mainland operations, which are categorized by the Corporation as consumer loans. The deterioration in the delinquency profile and the declines in property values have negatively impacted charge-offs.

… The allowance for loan losses represented 3.43% of loans held-in-portfolio at December 31, 2008, compared with 2.76% at September 30, 2008 and 1.96% at December 31, 2007. As of December 31, 2008, there were $898 million of SFAS No. 114 impaired loans in the Corporation's continuing operations with a related specific allowance for loan losses of $195 million, compared with impaired loans of $291 million and a specific allowance of $53 million as of December 31, 2007, excluding PFH.

During the quarter ended December 31, 2008, the Corporation recorded $150 million in provision for loan losses for loans classified as impaired under SFAS No. 114. As of September 30, 2008, there were $753 million of SFAS No. 114 impaired loans in the Corporation's continuing operations with a related specific allowance for loan losses of $131 million.

Non-performing assets of the continuing operations totaled $1.3 billion at December 31, 2008. This represented an increase of $192 million since September 30, 2008 primarily related to increases in construction loans by $84 million, mortgage loans by $57 million, commercial loans by $24 million, consumer loans by $10 million and other real estate by $17 million. Non- performing assets from continuing operations increased by $672 million from December 31, 2007 to the same date in 2008. The

increases were mostly reflected in commercial loans by $207 million, construction loans by $230 million, mortgage loans by $168 million, consumer loans by $26 million and other real estate by $40 million.

* * * *

Income Taxes

Income tax expense from continuing operations amounted to $309.1 million for the quarter ended December 31, 2008, compared with an income tax benefit of $15.4 million for the same quarter of 2007. ***As previously indicated, the variance was primarily due to the establishment of a full valuation allowance on the deferred tax assets of the U.S. mainland operations, as well as the impact of higher operating losses.***

The Corporation's net deferred tax assets (prior to deducting the valuation allowance) amounted to $1.2 billion as of December 31, 2008, of which $848 million pertains to the U.S. mainland operations. As of December 31, 2008, the Corporation recorded a total valuation allowance of $861 million on the deferred tax assets of the Corporation's U.S. operations. This full valuation allowance was recorded in consideration of the requirements of SFAS No. 109 "Accounting for Income Taxes" ("SFAS No. 109") which states that a deferred tax asset should be reduced by a valuation allowance ***if based on the weight of all available evidence, it is more likely than not (a likelihood of more than 50%) that some portion or all of the deferred tax asset will not be realized.*** The determination of whether a deferred tax asset is realizable is ***based*** on weighting all available evidence, including both positive and negative evidence. SFAS No. 109 provides that the realization of deferred tax assets, including carryforwards and deductible temporary differences, depends upon the existence of sufficient taxable income of the same character during the carryback or carryforward period. SFAS No. 109 requires the consideration of all sources of taxable income available to realize the deferred tax asset, including the future reversal of existing temporary differences, future taxable income exclusive of reversing temporary differences and carryforwards, taxable income in carryback years and tax planning strategies.

The Corporation's U.S. mainland operations are in a cumulative loss position for the three-year period ended December 31, 2008. For purposes of assessing the realizability of the deferred tax assets in the U.S. mainland, this cumulative taxable loss position, along with the evaluation of all sources of taxable income available to realize the deferred tax asset, as discussed above, is considered significant negative evidence and has caused management to conclude that the Corporation will not be able to fully realize the deferred tax assets in the future, considering solely the criteria of SFAS No. 109. Management will reassess the realizability of the deferred tax assets based on the criteria of SFAS No. 109 each reporting period. If future events differ from management's year-end 2008 assessment, a partial reversal of the valuation allowance may be required in future years. An important consideration, although not sufficient positive evidence to overcome the negative evidence under SFAS No. 109, is that the net operating loss carryforwards of the Corporation's U.S. operations have an expiration term of 20 years. To the extent that the financial results of the U.S. operations improve and the deferred tax asset becomes realizable, the Corporation will be able to reduce the valuation allowance through earnings.

(Emphasis added.)

210. In response to these disclosures, shares of the Company's common stock fell $2.52 per share, or 50%, to close at $ 2.46 per share, on heavy trading volume, and the Company lost over 50% of its market capitalization.

211. On February 19, 2009, the Individual Defendants also caused Popular to further reduce its quarterly dividend to $0.02, a 75 % reduction to the previous quarterly dividend payment rate of $0.08 cents per quarter that had been established with the 50% dividend cut (from $0.16 cents per share) announced in August 2008. As a result, Popular's common stock again fell an additional 11% in a single day, from $1.79 to $1.59, and Popular's Series B stock fell 43% in a single day, from $14 to $8.

212. Thereafter, on May 18, 2009, Fitch Ratings put Popular's and its subsidiaries' ratings on "Rating Watch Negative," stating "[t]oday's actions reflect Fitch's view that these institutions show an incrementally higher level of vulnerability to the credit deterioration which Fitch expects to continue across virtually all loan categories."

213. Citing the Company's deteriorating financial condition, on May 21, 2009, the Individual Defendants were forced to announce that Popular was in the process of shuttering more than 20% of its U.S. branch network to cut costs.

214. Finally, on September 18, 2009, the Individual Defendants allowed and/or caused Popular to announce that it will delist its Series A and Series B preferred stock from Nasdaq.

G. Defendants Breached Their Fiduciary Duties By Allowing Popular to Conduct Its Series B Offering Based on False and Misleading Offering Documents

215. On May 6, 2008, the Individual Defendants allowed and/or caused Popular to announce that it was "planning to commence a public offering of $350 million of non-cumulative perpetual preferred stock pursuant to an existing effective Popular registration statement." The registration statement, previously signed by Individual Defendants Carrión, Bermúdez, Ferré, Masin, Morales, Rexach, Salerno, Teuber, Vizcarrondo, and Junquera, as well as certified by Defendant PwC, on October 22, 2007 and declared effective by the SEC, expressly incorporated by reference "[a]ll documents that we file subsequent to the date of this prospectus and prior to the termination of

the offering of our common stock contemplated hereby pursuant to Section 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 . . . ."

216. Thereafter, on May 22, 2008, the Individual Defendants allowed and/or caused the Company to price the previously announced public offering of non-cumulative perpetual preferred stock offering and to increase the offering size by $50 million to $400 million. According to the Company's release issued that day, the "resulting offering of 16,000,000 shares was priced at 8.25% with a purchase price of $25 per share" and that it would be completed on May 28, 2008. Because the Offering Documents issued in connection with the preferred stock offering were false and misleading for the reasons detailed herein, in particular the failure to record a proper valuation allowance which inflated the earnings reported in the Offering Documents, Popular is now exposed to hundreds of millions of dollars in potential strict liability damages and/or rescission to the purchasers of these preferred shares for the misstatements alleged herein under §11 of the Securities Act of 1933.

217. None of the Defendants made a reasonable investigation or possessed reasonable grounds for the belief that the statements contained in the Offering Documents were accurate and complete in all material respects. Due diligence is a critical component of the issuing and underwriting process. Defendants were and are able to perform due diligence because of their expertise and access to the Company's non-public information.

218. Public investors, creditors and others rely on independent, registered public accounting firms to audit financial statements and assess internal controls when deciding whether to invest in or do business with a public company. Defendant PwC, the accounting firm which consented to the inclusion of its opinion in the Offering Documents, failed to perform its audit of Popular in a reasonable manner; and did not comply with Generally Accepted Auditing Standards ("GAAS's");[4] audit did not constitute a reasonable investigation of whether the Company's financial

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[4] The Public Company Accounting Oversight Board ("PCAOB"), established by the Sarbanes- Oxley Act of 2002, is responsible for the development of auditing and related professional practice standards that must be followed by

statements were presented in compliance with GAAP and management's assessment of internal controls was properly and accurately presented.

219. Specifically, during the Relevant Period, PwC issued a clean, unqualified audit opinion on the Company's financial statements for the years ending December 31, 2006 and December 31, 2007. PwC also consented to the incorporation by reference in the prospectus supplement for the Offering of its clean and unqualified audit opinion letter on the Company's financial statements for the years ending December 31, 2006 and December 31, 2007. In its opinion letter, PwC stated that it performed its audits and evaluations in accordance with the standards of the PCAOB, or GAAS. This statement was materially misstated when made and at the time of the Offering, as PwC's audit failed to comply with GAAS.

220. In certifying Popular's 2006 and 2007 financial statements, PwC specifically represented that those financial statements were prepared in accordance with GAAP and that PwC's audits were conducted in accordance with the standards of the PCAOB, or GAAS. These statements were materially untrue when made because the Individual Defendants failed to record a proper valuation allowance in those filings, thereby inflating the Company's earnings. When an auditor represents that a company's financial statements conform in all material respects with GAAP, the auditor "indicates [his] belief that the financial statements taken as a whole are not materially misstated." AU § 312.5 Indeed, "[f]inancial statements are materially misstated when they contain misstatements whose effect, individually or in the aggregate, is important enough to cause them not to be presented fairly, in all material respects, in conformity with [GAAP]." AU § 312.

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registered public accounting firms. On April 16, 2003, the PCAOB adopted as its interim standards GAAS as described by the AICPA Auditing Standards Board's SAS No. 95, "Generally Accepted Auditing Standards," and related interpretations in existence on that date. Accordingly, an auditor's reference to "the standards of the Public Accounting Oversight Board (United States)" includes a reference to GAAS in existence as of April 16, 2003. All references to GAAS hereinafter include PCAOB standards.

[5] GAAS includes Statements on Auditing Standards ("SAS") issued by the Auditing Standards Board of the American Institute of Certified Public Accountants ("AICPA"), which are codified in AICPA Professional Standards under the prefix "AU."

221. PwC's statements were similarly materially misstated because its audits did not conform to GAAS. Specifically, PwC was responsible for auditing whether the Company properly applied the provisions of SFAS 109.

222. Indeed, PwC's 2006 and 2007 audit reports specifically stated that "[o]ur audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation." Had PwC properly analyzed the Individual Defendants' application of SFAS 109 and actually examined evidence supporting the deferred tax asset amount in the Company's financial statements, the only reasonable professional conclusion was that the Company's deferred tax assets were overstated and its valuation allowance understated.

223. GAAS General Standard No. 3 requires an auditor to exercise due professional care in the performance of the audit and preparation of the report. AU § 150.02. PwC violated General Standard No. 3 by, among other things, disregarding Popular U.S.'s materially growing deferred tax asset and simultaneously shrinking U.S. operations and income, and the lack of a sufficient valuation allowance, and three year cumulative loss. Had PwC complied with GAAS, the only reasonable professional conclusion it could have drawn was that the Individual Defendants' valuation allowance for Popular's deferred tax assets was insufficient and, consequently, the Company had overstated its net income and the value of its assets in violation of GAAP.

224. GAAS Standard of Fieldwork No. 1 requires an auditor to plan the audit, which "involves developing an overall strategy for the expected conduct and scope of the audit." AU § 311.03. This requires understanding the entity's business sufficiently to identify areas of risk. AU §311.06. PwC violated Standard of Fieldwork No. 1 by, among other things, failing to plan and conduct an audit that would include identifying and assessing PwC's areas of risk, specifically, its deferred tax asset amount. Had PwC complied with GAAS, the only reasonable professional conclusion it could have drawn was that the Individual Defendants improperly failed to record an adequate valuation allowance for its deferred tax assets.

225. GAAS Standards of Fieldwork Nos. 2 and 3 require that an independent auditor obtain, through inspection, observation, inquiries and confirmations, competent, sufficient evidential matter to afford a reasonable basis for its opinion. AU § 150.02. PwC violated Standard of Fieldwork Nos. 2 and 3 by, among other things, failing to obtain evidence that Popular U.S. had sufficient future taxable income to support its failure to establish an adequate valuation allowance and later to establish that Popular's purported tax strategies were feasible and within management's control. Had PwC complied with GAAS, the only reasonable professional conclusion it could have drawn was that Popular's U.S.'s taxable income was insufficient to support its failure to establish an adequate valuation allowance and that its tax strategies were neither feasible, nor within the Company's and the Individual Defendants' control in violation of GAAP.

226. Standard of Reporting No. 4 requires an auditor to express an opinion on the financial statements of a company taken as a whole, or to state that an opinion cannot be expressed. AU § 150.02. As a result of PwC's violations of GAAS set forth above, it also violated the Standard of Reporting No. 4 because PwC had an insufficient basis to express an unqualified opinion on its 2006 and 2007 audit of Popular. Accordingly, as set forth above, PwC's public statements concerning those audits were untrue and contained omissions of material facts.

227. Notably, the Individual Defendants' accounting under SFAS 109 was in violation of PwC's own "Guide to Accounting for Income Taxes."

228. In particular, PwC allowed the Individual Defendants to record Popular U.S.'s deferred tax assets without any valuation allowance despite the fact that the Individual Defendants were already planning to significantly downsize Popular U.S.'s operations and that Popular U.S. was already in a cumulative loss position at the beginning of 2008 and the Relevant Period. PwC did so even though Popular did not present any evidence to counterbalance Popular U.S.'s cumulative loss. Further, PwC did so, even though it recognized in its own tax guide that Popular could not avoid a valuation allowance merely by relying on projections of future income within the standard 20-year duration of the assets:

> A projection of future taxable income is inherently subjective and generally will not be sufficient to overcome negative evidence that includes cumulative losses in recent years, particularly if the projected future taxable income is dependent on an anticipated turnaround to operating profitability that has not yet been demonstrated." PwC "Guide to Accounting for Income Taxes" at 93 (2007).

229. In addition, PwC's own tax guide provides that a company, like Popular, that was relying on restructuring plans to reduce costs and potentially return to profitability, should have taken a valuation allowance against its deferred tax assets due to a three year cumulative loss:

> An enterprise with significant negative evidence, such as a history of recent losses, normally will find it very difficult to demonstrate that even an implemented exit plan provides sufficient objective evidence that the enterprise will be restored to profitability, prior to the time that it actually becomes profitable. In these circumstances, it would be that much more difficult to demonstrate that an unimplemented exit plan provides sufficient evidence to overcome the negative evidence present.

230. On September 18, 2009, the Individual Defendants allowed and/or caused Popular to announce that it would delist its Series B preferred stock from Nasdaq. By allowing the Series B Offering based on false and misleading Offering Documents, Defendants have exposed the Company to liability under the Securities Act of 1933.

RULE 23.1 DERIVATIVE AND DEMAND FUTILITY ALLEGATIONS

231. Plaintiff hereby incorporates ¶¶ 1-230 above.

232. Plaintiff is currently beneficial or record owner of 2,077 shares of common stock, and has continuously held an equity interest in the shares of Popular at all times relevant hereto, and has standing to bring this derivative action.

233. Plaintiff brings this action derivatively in the right of and for the benefit of the Company to redress injuries suffered by the Company as a direct result of Defendants' wrongdoing. This is not a collusive action to confer jurisdiction on this Court which it would not otherwise have. Plaintiff will adequately and fairly represent the interests of Popular and its shareholders in enforcing and prosecuting their rights.

A. **Plaintiff Is Excused From Making a Demand Since Popular's Board Knew About the Wrongdoing**

234. The Board (or at the very least a majority of it) cannot exercise independent objective judgment about whether to bring this action or whether to vigorously prosecute this action. For the reasons that follow in ¶¶ 235- 250 of this Complaint, and for reasons detailed elsewhere in this Complaint, Plaintiff has not made (and should be excused from making) a pre-filing demand on the Board to initiate this action because making a demand would be a futile and useless act.

235. The acts complained of herein constitute violations of fiduciary duties of good faith, loyalty, and candor owed by the Board to the Company and its shareholders.

236. The Board cannot be relied upon to reach a truly independent decision as to whether to consider a demand for action against themselves and the officers responsible for the misconduct alleged in this Complaint, in that, *inter alia*, the Board is dominated by Defendant Carrión who was personally and directly involved in the misconduct alleged and/or who approved the actions complained of here. This domination of the Board has impaired the Board's ability to validly exercise its business judgment and rendered it incapable of reaching an independent decision as to whether to accept Plaintiff's demand.

237. Although the members of the Popular Board were required, pursuant to their fiduciary duties as Popular Board members and as members of specific committees of the Company's Board, to monitor and ensure that the operations of the Company were based on sound business judgment, the members of the Popular Board failed to exercise their duties, and rather, simply deferred their judgment to Individual Defendants Carrión and Junquera, thereby causing and/or permitting Popular to engage in the reckless and misleading conduct described above, exposing the Company to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments and defense costs and reputational harm.

238. In order to bring this action for breaching their fiduciary duties, each of the Director Defendants would have to sue himself/herself and/or his/her fellow directors and allies in the top ranks of the Company, who are his/her good friends and with whom he/she has entangling financial

alliances, interests and dependencies, and to expose each of them to a substantial risk of liability which each director of the Board would not do. Therefore, the Board would not be able to vigorously prosecute any such action and cannot in good faith exercise independent business judgment to determine whether to bring this action against themselves and one another.

239. Because of their participation in the mismanagement of the Company, gross dereliction of fiduciary duties, breaches of the duties of good faith and loyalty, waste of Popular's corporate assets, and abuse of their control of Popular, the Director Defendants are unable to comply with their fiduciary duties and prosecute this action. Each of them is in a position of irreconcilable conflict of interest in terms of the prosecution of this action and defending themselves in the securities class action lawsuit brought under the Securities Exchange Act of 1934 and the Securities Act of 1933, and the class action brought under ERISA.

240. Additionally, each of the Director Defendants named herein received payments, benefits, stock options and other emoluments by virtue of their membership on the Board and their control of Popular. They have thus benefited from the wrongdoing herein alleged and have engaged in such conduct to preserve their positions of control and the perquisites thereof, and are incapable of exercising independent objective judgment in deciding whether to bring this action.

241. Further, the Company's current and past officers and directors are protected against personal liability for their acts of mismanagement, waste, and breach of fiduciary duty alleged in this Complaint by directors' and officers' liability insurance, which they caused the Company to purchase with corporate funds for their protection – monies belonging to Popular stockholders. However, due to certain changes in the language of directors' and officers' liability insurance policies in the past few years, the directors' and officers' liability insurance policies covering the Director Defendants in this case contain provisions which eliminate coverage for any action brought directly by Popular against these members of the Popular Board, known as, *inter alia*, the "insured versus insured exclusion." As a result, if the Director Defendants were to sue themselves or certain Company officers, there would be no directors' and officers' insurance protection and thus, this is a further reason why they will not bring such a suit. On the other hand, if the suit is brought

derivatively, as this action is brought, such insurance coverage exists and will provide a basis for the Company to effect a recovery.

242. As of the filing of this Complaint, the current Popular Board of Directors consists of nine (9) members; they are Defendants Carrión, Bermúdez, Ferré, Masin, Morales, Rexach, Salerno, Teuber and Vizcarrondo. All Director Defendants were directors at Popular during the entire Relevant Period.

243. The following Popular Board members named as Director Defendants are incapable of independently and disinterestedly considering a demand to commence and vigorously prosecute this action because the following facts, taken collectively, demonstrate that they are riddled in conflicts and face substantial likelihood of liability:

a. Defendant Carrión is incapable of considering a demand because;

   i. as the Company readily acknowledges, he is not independent under the Nasdaq independence standards, because of employment at Popular and his personal, professional, and financial entanglements with other defendants and the Company;

   ii. he was the CEO and President of the Company the entire time that Popular improperly accounted for its deferred tax assets and conducted the $400 million preferred stock offering utilizing a registration statement he knew contained false and misleading statements, and he was responsible for directing the Company's day-to-day operations and for overseeing its corporate development and strategic planning;

   iii. he is the uncle of fellow Board member and Director Defendant Vizcarrondo and Popular concedes the close familiar relationship impairs both defendants' independence;

   iv. he is further beholden to the Company, which further impairs his independence, because another one of his nephews is employed as a Vice President in the Merchant Business Administration Division of the Bank;

   v. he knew and approved the Company's unlawful and unethical plan to improperly account for $525 million worth of deferred tax assets and conduct the $400 million preferred stock offering utilizing a registration statement he knew contained false and misleading statements;

   vi. Carrión has served as a director of Verizon Communications, Inc. since 1995, where Salerno served as vice chairman and chief financial officer until 2002.

By virtue of their long-term personal, professional and financial relationships, including the fact that Carrión oversaw Salerno's livelihood and compensation for many years, Carrión could not impartially investigate and/or prosecute the misconduct alleged herein against Salerno, who was the chairperson and financial expert of the Audit Committee and who was responsible for reviewing and overseeing the Company's financial statements throughout the Relevant Period;

vii. he certified all the SEC filings (*e.g.*, Form 10-K and quarterly reports for years 2007, 2008 and 2009) and the offering Documents that contained misleading information about the Company's deferred tax assets in violation of federal securities laws;

viii. he is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both before this Court – substantially increasing Carrión's likelihood of liability; and

ix. he is a defendant in this action and there is reasonable doubt that Carrión is capable of independently considering a demand to pursue this action on behalf of the Company because Carrión himself faces a substantial likelihood of liability for his actions.

b. Defendant Bermúdez is incapable of considering a demand because,

i. he is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both this Court – substantially increasing Bermúdez's likelihood of liability;

ii. he faces a substantial likelihood of liability in the *Hoff* securities class action because he signed the Company's materially misstated Offering Documents, which are the subject of the *Hoff* action, through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering;

iii. as Chairman of the Trust Committee of the Bank since 1996, he was charged with a higher degree of oversight over Popular's day-to-day operations than a traditional "outside director" would be and as such, he faces increased exposure to personal liability;

iv. by allowing and/or causing Popular to violate GAAP by improperly accounting for nearly $1 billion of gross deferred tax assets and conduct the $400 million preferred stock Offering utilizing a registration statement he knew contained false and misleading statements, he failed to meet his responsibilities as a member of the Audit Committee, which is charged with overseeing the integrity of Popular's financial statements. Thus, he faces a substantial likelihood of liability for his actions and inaction. Specifically, he failed to adequately review the Company's financial statements as such that the Company had no reasonable basis for failing to record valuation allowance

during the Relevant Period in the face of a substantial amount of negative evidence concerning Popular U.S.'s ability to earn future taxable income, breaching his fiduciary duties. Bermúdez is thereby disabled from performing a disinterested view of the claims in this case, and from acting to bring a suit and remedy the wrongs described herein. He either actually knew of the improper accounting for the deferred tax assets, and the plan to engage in false and material misrepresentations to investors, or he breached his fiduciary duties by recklessly disregarding his obligations by failing to monitor the financial operations of the Company. By failing to perform proper due diligence and inform himself about and oversee the Company's affairs, he exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments and defense costs and reputational harm;

v. he also failed to meet his responsibilities as a member of the Audit Committee, which is also charged with overseeing the outside auditors' qualifications. Here, he failed to fulfill that responsibility because he allowed the Company to use PwC as its auditor. PwC clearly violated GAAS, did not comply with standards of the Public Company Accounting Oversight Board ("PCAOB"); did not comply with PwC's own published audit guidance ("Accounting for Income Taxes"); and its audit did not constitute a reasonable investigation of whether the Company's financial statements were presented in compliance with GAAP. Thus, he faces a substantial likelihood of liability for his actions and inaction;

vi. by allowing and/or causing Popular to incentivize risk-taking and financial misreporting by its senior executives and employees, he failed to meet his responsibilities as a member of the Compensation Committee, which is charged with reviewing and assessing incentive compensation arrangements to ensure that they do not encourage senior executive officers to take unnecessary and excessive risks that may threaten the value of the Company. He rewarded the risk-taking and misreporting concerning the deferred tax assets, as discussed herein, by awarding Individual Defendants Carrión, Chafey, Junquera and Herencia significant short-term incentives and steadily increasing salaries, as detailed in ¶¶ 67-79. Furthermore, he rewarded Herencia's poor management of BPNA by approving an excessive and unwarranted $3.2 severance payment. In light of having caused Popular to incentivize reckless risk-taking during the Relevant Period, he breached his fiduciary duties and exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments, defense costs and reputational harm. Thus, he faces a substantial likelihood of liability for his actions; and

vii. he is a defendant in this action and there is reasonable doubt that Bermúdez is capable of independently considering a demand to pursue this action on behalf of the Company because Bermúdez himself faces a substantial likelihood of liability for his actions.

c. Defendant Ferré is incapable of considering a demand because,

i. she is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both before this Court – substantially increasing Ferré's likelihood of liability;

ii. she faces a substantial likelihood of liability in the *Hoff* securities class action because she signed the Company's materially misstated Offering Documents, which are the subject of the *Hoff* action, through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering;

iii. she is a is the president and a trustee of the Fundación Luis A. Ferré, a foundation. In December 2005, the Bank entered into a commitment to contribute a total of $500,000 to the Fundación Luis A. Ferré during a period of five years in connection with the remodeling of the Ponce Museum of Art premises. The first payment in the amount of $100,000 was made in November 2006. The second payment in the amount of $100,000 was made in December 2007. The third payment in the amount of $100,000 was made in December 2008. In 2006 and 2008, the Bank also made a contribution of $50,000 ($150,000 in total) to the Fundación Luis A. Ferré in connection with the sponsorship of the Ponce Museum of Art Benefit Gala. By virtue of the fact that Ferré is employed and derives her livelihood from the foundation, a significant beneficiary of Popular, Ferré's independence is compromised and she would be unable to comply with fiduciary duties to Popular and its investors in diligently investigating and prosecuting the claims alleged herein against Carrión or any of the other Director Defendants that approved of this transaction;

iv. by allowing and/or causing Popular to incentivize risk-taking and financial misreporting by its senior executives and employees, she failed to meet her responsibilities as a member of the Compensation Committee, which is charged with reviewing and assessing incentive compensation arrangements to ensure that they do not encourage senior executive officers to take unnecessary and excessive risks that may threaten the value of the Company. She rewarded the risk-taking and misreporting concerning the deferred tax assets, as discussed herein, by awarding Individual Defendants Carrión, Chafey, Junquera and Herencia significant short-term incentives and steadily increasing salaries, as detailed in ¶¶ 67-79. Furthermore, she rewarded Herencia's poor management of BPNA by approving an excessive and unwarranted $3.2 severance payment. In light of having caused Popular to incentivize reckless risk-taking during the Relevant Period, she breached her fiduciary duties and exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments, defense costs and reputational harm. Thus, she faces a substantial likelihood of liability for her actions; and

v. she is a defendant in this action and there is reasonable doubt that Ferré is capable of independently considering a demand to pursue this action on behalf of the Company because Ferré herself faces a substantial likelihood of liability for her actions.

d. Defendant Masin is incapable of considering a demand because,

i. he is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both before this Court – substantially increasing Masin's likelihood of liability;

ii. he faces a substantial likelihood of liability in the *Hoff* securities class action because he signed the Company's materially misstated Offering Documents, which are the subject of the *Hoff* action, through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering;

iii. he served as vice chairman and chief operating officer of Citigroup from 2002 to 2004 and has served as a trustee of the Weill Family Foundation since 2002. Citigroup and Popular Securities served as co-underwriters for scores of public offerings during the Relevant Period. By virtue of his personal, professional and financial relationships with the executives at Citigroup and Popular, Masin is disabled from complying with his fiduciary duties and diligently investigating and prosecuting the claims alleged herein;

iv. he was also a senior partner at the international law firm of O'Melveny & Myers until February 2008. The law firm's website boasts that its "corporate finance lawyers represent some of the largest and most sophisticated private equity firms, corporations, banks and investment funds, as borrowers and lenders, issuers and investors, in financing and debt investing transactions in the principal debt markets in the United States, Asia, and Europe" and lists as practice specialties "asset-based financings, bridge loans, corporate credit facilities, distressed debt investing, high yield bond financings, investment credit facilities, letter of credit facilities, leveraged acquisition and recapitalization financings, mezzanine debt financings, private placements, senior secured credit facilities, subordination and intercreditor arrangements, venture debt financing and workouts and restructurings," all of which would put O'Melveny & Myers' partners in constant contact with Popular Securities. Though Masin left O'Melveny & Myers in February 2008, upon information and belief, he retains a financial interest in O'Melveny & Myers' profits and maintains long-term personal, professional and financial ties with the firm's partners and its clients. As such, Individual Defendant Masin's ability to diligently investigate and prosecute the claims alleged herein would be unduly impeded as doing so would threaten his livelihood and financial interests; and

v. he is a defendant in this action and there is reasonable doubt that Masin is capable of independently considering a demand to pursue this action on behalf

of the Company because Masin himself faces a substantial likelihood of liability for his actions.

e. Defendant Morales is incapable of considering a demand because,

i. he is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both which is before this Court – substantially increasing Morales' likelihood of liability;

ii. he faces a substantial likelihood of liability in the *Hoff* securities class action because he signed the Company's materially misstated Offering Documents, which are the subject of the *Hoff* action, through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering;

iii. he is beholden to the Company, which impairs his independence, because his son is employed as Senior Vice President of the Ticketpop Networks Division of EVERTEC, Inc. (a subsidiary of Popular). He received compensation in the amount of approximately $196,422 during 2008; $255,000 in 2007and $255,631 in 2006;

iv. he and Carrión have served on the Board of Trustees of Fundación Banco Popular, Inc. together since 1982. Morales has also served as president of Parkview Realty, Inc. since 1985, the Atrium Office Center, Inc. since 1996, HQ Business Center P.R., Inc. since 1995, and other entities engaged in real estate leasing. By virtue of the fact that Morales' livelihood is incumbent upon building and maintaining relationships with executives like Carrión and the executives of other banks and firms engaged in the real estate industry, and Morales' long-term personal, professional and financial ties to Carrión, Morales cannot independently investigate or prosecute the claims alleged herein against Carrión or the other Director Defendants beholden to Carrión as it would be against his economic self-interest to do so;

v. by allowing and/or causing Popular to incentivize risk-taking and financial misreporting by its senior executives and employees, he failed to meet his responsibilities as a member of the Compensation Committee, which is charged with reviewing and assessing incentive compensation arrangements to ensure that they do not encourage senior executive officers to take unnecessary and excessive risks that may threaten the value of the Company. He rewarded the risk-taking and misreporting concerning the deferred tax assets, as discussed herein, by awarding Individual Defendants Carrión, Chafey, Junquera and Herencia significant short-term incentives and steadily increasing salaries, as detailed in ¶¶ 67-79. Furthermore, he rewarded Herencia's poor management of BPNA by approving an excessive and unwarranted $3.2 severance payment. In light of having caused Popular to incentivize reckless risk-taking during the Relevant Period, he breached his fiduciary duties and

exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments, defense costs and reputational harm. Thus, he faces a substantial likelihood of liability for his actions; and

vi. he is a defendant in this action and there is reasonable doubt that Morales is capable of independently considering a demand to pursue this action on behalf of the Company because Morales himself faces a substantial likelihood of liability for his actions.

f. Defendant Rexach is incapable of considering a demand because,

i. he is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both before this Court – substantially increasing Rexach's likelihood of liability;

ii. he faces a substantial likelihood of liability in the *Hoff* securities class action because he signed the Company's materially misstated Offering Documents, which are the subject of the *Hoff* action, through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering;

iii. he also serves as a Director of the Bank, Popular International Bank, Inc., Popular North America, Inc., Banco Popular North America, Banco Popular de Puerto Rico, Popular Cash Express, Inc. and Equity One, Inc. By virtue of these other directorships, Rexach is charged with a higher degree of knowledge, skill and oversight over Popular's day-to-day operations than a traditional "outside director" would be and as such, Rexach faces increased exposure to personal liability if the claims alleged herein are prosecuted;

iv. he is also beholden to the Company, which impairs his independence, because his two sons and a daughter-in-law are employed as Vice President of the Business Banking Division of the Bank, Project Coordinator of the Product Development area in the Card Products Division of the Bank, and as an Assistant Vice President of the Trust Division of the Bank, respectively, and received compensation during 2008 of approximately the aggregate amount of \$223,000, \$195,000 in 2007; and \$151,264 in 2006;

v. by allowing and/or causing Popular to violate GAAP by improperly accounting for nearly \$1 billion of gross deferred tax assets and conduct the \$400 million preferred stock offering utilizing a registration statement he knew contained false and misleading statements, he failed to meet his responsibilities as a member of the Audit Committee, which is charged with overseeing the integrity of Popular's financial statements. Thus, he faces a substantial likelihood of liability for his actions and inaction. Specifically, he failed to adequately review the Company's financial statements as such that the Company had no reasonable basis for failing to record valuation allowance

during the Relevant Period in the face of a substantial amount of negative evidence concerning Popular U.S.'s ability to earn future taxable income,, breaching his fiduciary duties. Rexach is thereby disabled from performing a disinterested view of the claims in this case, and from acting to bring a suit and remedy the wrongs described herein. He either actually knew of the improper accounting for the deferred tax assets, and the plan to engage in false and material misrepresentations to investors, or he breached his fiduciary duties by recklessly disregarding his obligations by failing to monitor the financial operations of the Company. By failing to perform proper due diligence and inform himself about and oversee the Company's affairs, he exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments and defense costs and reputational harm;

vi. he also failed to meet his responsibilities as a member of the Audit Committee, which is also charged with overseeing the outside auditors' qualifications. Here, he failed to fulfill that responsibility because he allowed the Company to use PwC as its auditor. PwC clearly violated GAAS, did not comply with standards of the PCAOB; did not comply with PwC's own published audit guidance ("Accounting for Income Taxes"); and its audit did not constitute a reasonable investigation of whether the Company's financial statements were presented in compliance with GAAP. Thus, he faces a substantial likelihood of liability for his actions and inaction;

vii. by allowing and/or causing Popular to incentivize risk-taking and financial misreporting by its senior executives and employees, he failed to meet his responsibilities as a member of the Compensation Committee, which is charged with reviewing and assessing incentive compensation arrangements to ensure that they do not encourage senior executive officers to take unnecessary and excessive risks that may threaten the value of the Company. He rewarded the risk-taking and misreporting concerning the deferred tax assets, as discussed herein, by awarding Individual Defendants Carrión, Chafey, Junquera and Herencia significant short-term incentives and steadily increasing salaries, as detailed in ¶¶ 67-79. Furthermore, he rewarded Herencia's poor management of BPNA by approving an excessive and unwarranted $3.2 severance payment. In light of having caused Popular to incentivize reckless risk-taking during the Relevant Period, he breached his fiduciary duties and exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments, defense costs and reputational harm. Thus, he faces a substantial likelihood of liability for his actions; and

viii. he is a defendant in this action and there is reasonable doubt that Rexach is capable of independently considering a demand to pursue this action on behalf of the Company because Rexach himself faces a substantial likelihood of liability for his actions.

g. Defendant Salerno is incapable of considering a demand because,

i. he is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both before this Court – substantially increasing Salerno's likelihood of liability;

ii. he faces a substantial likelihood of liability in the *Hoff* securities class action because he signed the Company's materially misstated Offering Documents, which are the subject of the *Hoff* action, through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering;

iii. Carrión has served as a director of Verizon Communications, Inc. since 1995, where Salerno served as vice chairman and chief financial officer until 2002. By virtue of their long-term personal, professional and financial relationships, including the fact that Carrión oversaw Salerno's livelihood and compensation for many years, Salerno is beholden to Carrión and could not impartially investigate and/or prosecute the misconduct alleged herein;;

iv. by allowing and/or causing Popular to violate GAAP by improperly accounting for nearly $1 billion of gross deferred tax assets and conduct the $400 million preferred stock offering utilizing a registration statement he knew contained false and misleading statements, he failed to meet his responsibilities as the ***chairperson and financial expert*** of the Audit Committee, which is charged with overseeing the integrity of Popular's financial statements. Despite his designation as a financial expert, Salerno failed to identify and remedy this glaring accounting error. Thus, he faces a substantial likelihood of liability for his actions and inaction. Specifically, he failed to adequately review the Company's financial statements as such that the Company had no reasonable basis for failing to record valuation allowance during the Relevant Period in the face of a substantial amount of negative evidence concerning Popular U.S.'s ability to earn future taxable income, breaching his fiduciary duties. Salerno is thereby disabled from performing a disinterested view of the claims in this case, and from acting to bring a suit and remedy the wrongs described herein. He either actually knew of the improper accounting for the deferred tax assets, and the plan to engage in false and material misrepresentations to investors, or he breached his fiduciary duties by recklessly disregarding his obligations by failing to monitor the financial operations of the Company. By failing to perform proper due diligence and inform himself about and oversee the Company's affairs, he exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments and defense costs and reputational harm;

v. he also failed to meet his responsibilities as a member of the Audit Committee, which is also charged with overseeing the outside auditors' qualifications. Here, failed to fulfill that responsibility because he allowed the Company to use PwC as its auditor. PwC clearly violated GAAS, did not comply with standards of the Public Company Accounting Oversight Board ("PCAOB"); did not comply with PwC's own published audit guidance ("Accounting for Income

Taxes"); and its audit did not constitute a reasonable investigation of whether the Company's financial statements were presented in compliance with GAAP. Thus, he faces a substantial likelihood of liability for his actions and inaction; and

vi. he is a defendant in this action and there is reasonable doubt that Salerno is capable of independently considering a demand to pursue this action on behalf of the Company because Salerno himself faces a substantial likelihood of liability for his actions.

h. Defendant Teuber is incapable of considering a demand because,

i. he is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both before this Court – substantially increasing Teuber's likelihood of liability;

ii. he faces a substantial likelihood of liability in the *Hoff* securities class action because he signed the Company's materially misstated Offering Documents, which are the subject of the *Hoff* action, through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering;

iii. by allowing and/or causing Popular to violate GAAP by improperly accounting for nearly $1 billion of gross deferred tax assets and conduct the $400 million preferred stock offering utilizing a registration statement he knew contained false and misleading statements, he failed to meet his responsibilities as a member ***and financial expert*** of the Audit Committee, which is charged with overseeing the integrity of Popular's financial statements. Despite his designation as a financial expert, Teuber failed to identify and remedy this glaring accounting error. Thus, he faces a substantial likelihood of liability for his actions and inaction. Specifically, he failed to adequately review the Company's financial statements as such that the Company had no reasonable basis for failing to record valuation allowance during the Relevant Period in the face of a substantial amount of negative evidence concerning Popular U.S.'s ability to earn future taxable income, breaching his fiduciary duties. Teuber is thereby disabled from performing a disinterested view of the claims in this case, and from acting to bring a suit and remedy the wrongs described herein. He either actually knew of the improper accounting for the deferred tax assets, and the plan to engage in false and material misrepresentations to investors, or he breached his fiduciary duties by recklessly disregarding his obligations by failing to monitor the financial operations of the Company. By failing to perform proper due diligence and inform himself about and oversee the Company's affairs, he exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments and defense costs and reputational harm;

iv. he also failed to meet his responsibilities as a member of the Audit Committee, which is also charged with overseeing the outside auditors' qualifications. Here, failed to fulfill that responsibility because he allowed the Company to use PwC as its auditor. PwC clearly violated GAAS, did not comply with standards of the Public Company Accounting Oversight Board ("PCAOB"); did not comply with PwC's own published audit guidance ("Accounting for Income Taxes"); and its audit did not constitute a reasonable investigation of whether the Company's financial statements were presented in compliance with GAAP. Thus, he faces a substantial likelihood of liability for his actions and inaction;

v. by allowing and/or causing Popular to incentivize risk-taking and financial misreporting by its senior executives and employees, he failed to meet his responsibilities as a member of the Compensation Committee, which is charged with reviewing and assessing incentive compensation arrangements to ensure that they do not encourage senior executive officers to take unnecessary and excessive risks that may threaten the value of the Company. He rewarded the risk-taking and misreporting concerning the deferred tax assets, as discussed herein, by awarding Individual Defendants Carrión, Chafey, Junquera and Herencia significant short-term incentives and steadily increasing salaries, as detailed in ¶¶ 69-73. Furthermore, he rewarded Herencia's poor management of BPNA by approving an excessive and unwarranted $3.2 severance payment. In light of having caused Popular to incentivize reckless risk-taking during the Relevant Period, he breached his fiduciary duties and exposed Popular to immense civil liability, including hundreds of millions of dollars in potential fines, penalties, civil judgments, defense costs and reputational harm. Thus, he faces a substantial likelihood of liability for his actions; and

vi. he is a defendant in this action and there is reasonable doubt that Teuber is capable of independently considering a demand to pursue this action on behalf of the Company because Teuber himself faces a substantial likelihood of liability for his actions.

i. Defendant Vizcarrondo is incapable of considering a demand because,

i. he is an individually named defendant in *Hoff v. Popular, Inc.,* 09-cv-1428-GAG and *In Re Popular, Inc. ERISA Litigation*, 09-cv-1552-ADC, which are both before this Court – substantially increasing Vizcarrondo's likelihood of liability;

ii. he faces a substantial likelihood of liability in the *Hoff* securities class action because he signed the Company's materially misstated Offering Documents, which are the subject of the *Hoff* action, through which Popular Series B preferred shares were offered and sold to the public during the Relevant Period, and was a Popular director at the time of the Series B Offering;

iii. he is the nephew of fellow Board member and Director Defendant Carrión and Popular concedes the close, familiar relationship impairs both defendants' independence;

iv. he is also beholden to the Company and fellow Director Defendants because Vizcarrondo as President, Chief Executive Officer and partner of Metropolitan Builders, S.E. (a special partnership organized under the laws of the Commonwealth of Puerto Rico) received two lucrative contracts from the Company, which were approved by the members of the Audit Committee. First, during 2006, the Company paid approximately $225,000 in connection with two Bank construction projects awarded to this entity in 2002. The Bank also paid approximately $51,000 in connection with the construction of a bridge connecting two of the Bank's buildings. In addition, during 2006 the Bank paid to Metropolitan Builders, S.E. approximately $887,000 in connection with two contracts for the interior partition and finishes of the two Bank construction projects;

v. he is further beholden to the Company, which further impairs his independence, because his brother is employed as a Vice President in the Merchant Business Administration Division of the Bank and received compensation of approximately $200,322 during 2008, $198,000 in 2007 and $148,904 in 2006;

vi. he has served as president, CEO and partner of Desarrollos Metropolitanos, L.L.C., a general construction company, since 2004, and as a member of the board of directors of the Puerto Rico Chapter of the National Association of Home Builders since 2002. By virtue of the fact that Vizcarrondo's livelihood is incumbent upon building and maintaining relationships with executives like Carrión and the executives of other banks and firms engaged in the Puerto Rico real estate industry, and Vizcarrondo's long-term personal, professional and financial ties to Carrión, Vizcarrondo cannot independently investigate or prosecute the claims alleged herein against Carrión or the other Director Defendants beholden to Carrión as it would be against his economic self-interest to do so;

vii. he served as a member of the Trust Committee of the Bank since 1996, and was charged with a higher degree of oversight over Popular's day-to-day operations than a traditional "outside director" would be and as such, he faces increased exposure to personal liability; and

viii. he is a defendant in this action and there is reasonable doubt that Vizcarrondo is capable of independently considering a demand to pursue this action on behalf of the Company because Vizcarrondo himself faces a substantial likelihood of liability for his actions.

244. In addition to the foregoing, demand is excused because the members of the Popular Board made a conscious business decision to breach their fiduciary duties by causing Popular to

improperly account for nearly $1 billion of deferred tax assets, conduct the $400 million preferred stock offering utilizing a registration statement they knew contained false and misleading statements caused the Company to commit violations of GAAP; and exposed Popular to immense liability under the federal securities laws and ERISA. Thus, Defendants' actions are not entitled to business judgment deference. Moreover, as demonstrated above (and summarized in the chart below), because each Director Defendant permitted and/or caused Popular to issue the false and misleading statements detailed above during the Relevant Period, and/or improvidently deferred judgment to Individual Defendants Carrión, Junquera and Chafey to whom a majority of the Director Defendants are beholden, a majority of the members of the Popular Board are not disinterested and independent, the alleged misconduct was not the product of their valid exercise of business judgment, and for these and the other reasons detailed herein, a presuit demand was not required as it would have been futile:

BOARD MEMBER/ DISABLING CONFLICT	SIGNED REG. STMNT.	AUDIT COMM. MEMB.	COMP. COMM. MEMB.	DISABLING THREAT TO LIVELIHOOD	DISABLING FAMILIAR RELATIONSHIPS	CROSS BOARD MEMBERSHIPS	INCREASED EXPOSURE TO PERSONAL LIABILITY
CARRIÓN	X			X	X	X1, X2, X3	X
JUNQUERA	X			X	X		X
MORALES	X		X	X	X	X1	X
REXACH	X	X	X		X		X
BERMÚDEZ	X	X	X				X
FERRÉ	X		X	X		X2	X
TEUBER	X	X	X				X
VIZCARRONDO	X			X	X		X
MASIN	X			X			X
SALERNO	X	X				X3	X

B. **The Director Defendants' Wrongful Acts Are Not Protected By The Business Judgment Rule.**

245. Furthermore, pre-suit demand on the Board would have been futile because the wrongs complained of herein were not, and could not have been, an exercise of good faith business judgment. Making a demand on the Board of Directors is excused if there is reasonable doubt that the challenged transactions were the product of a valid exercise of business judgment and, therefore,

are entitled to the protection of the business judgment rule. To benefit from the protection of the business judgment rule, a director must be informed of all material information reasonably available and, being so informed, the director must act with requisite care in discharging his or her duties. To meet the standard of care, in light of the information which the Director Defendants knew, they were obligated to take actions in the best interests of the Company, to the exclusion of their personal pecuniary interests, conduct full and adequate investigation into decisions affecting the Company and its assets, and ensure that the Company was in compliance with applicable laws and regulations.

246. The Director Defendants cannot defend their actions by any alleged "independent" business judgment since each of them acted in bad faith, grossly and recklessly abused their discretion, acted in breach of their fiduciary duties to the Company and its stockholders and failed to act and abdicated their functions and duties as directors. And because the Director Defendants engaged in acts of misconduct and wrongdoing, as described above, those acts were not the product of a valid exercise of business judgment and not entitled to the protections of the business judgment rule. The Director Defendants failed to act to protect the interests and business assets of Popular, and failed to ensure that Popular complied with relevant laws and regulations. Failure to take such protections and engagement in egregious unethical conduct could not have been a valid exercise of business judgment.

247. Demand is excused because, as detailed above, Director Defendants caused, or through a lack of reasonably prudent oversight allowed, the Company to continuously and systematically issue false and misleading statements regarding their deferred tax asset strategy and improperly inflated earnings in violation of GAAP. Accordingly, the Director Defendants' misconduct is egregious enough to reasonably conclude that it falls outside the protection of the business judgment rule, thereby excusing Plaintiff from bringing a pre-suit demand on futility grounds.

248. Further actions that support the fact that the Director Defendants' failure to ensure that Popular U.S.'s deferred tax assets were properly offset and that the Series B Offering did not use

false and misleading Offering Documents falls out of the business judgment rule, include the following "red flags:"

- Director Defendants recklessly disregarding the fact that, since as early as January 2007, the Company began to significantly downsize, restructure and sell poorly performing Popular U.S. operations. This severely limited Popular U.S.'s ability to produce the future taxable income necessary to realize the deferred tax assets it had recorded, which required the Company to record the proper valuation allowance. However, Director Defendants failed to record the proper valuation allowance by hundreds of millions of dollars throughout the Relevant Period in violation of GAAP;

- Director Defendants recklessly disregarding the fact that Popular U.S. experienced steadily deteriorating income since 2005, culminating in a three-year cumulative loss of roughly $646 million by the end of fiscal year 2007. These increasingly large successive losses made it more likely than not that Popular U.S. would have future taxable income which required the Company to record a full valuation allowance. However, Director Defendants failed to record the proper valuation allowance by hundreds of millions of dollars throughout the Relevant Period in violation of GAAP; and

- Director Defendants recklessly disregarding the fallout of the U.S. housing and financial markets that forced the Company to significantly increase its loan loss reserves. Furthermore, Director Defendants recklessly disregarding the fact that Popular U.S.'s construction and loan portfolios continued to deteriorate as the quality of its U.S. mortgages decreases and the number of non-performing loans continued to increase. The increase in its loan loss reserve and the continued deterioration of its U.S. loan portfolios were clear examples that Popular U.S. had no realistic prospects for earning future taxable income. However, Director Defendants failed to record the proper valuation allowance by hundreds of millions of dollars throughout the Relevant Period in violation of GAAP;

249. The magnitude and duration of these "red flags" demonstrate that the failure of the Director Defendants to act accordingly constitutes a lack of good faith and that their actions, or lack thereof, are not protected by the business judgment rule. Furthermore, by undertaking the Series B Offering utilizing a false and misleading registration statement and exposing the Company to hundreds of millions of dollars in potential ***strict*** liability under the Securities Act of 1933 was so reckless on its face that it could not have been the product of the Director Defendants' sound business judgment. In fact, each of Director Defendants signed the false and misleading registration statement and was thus responsible for ensuring its accuracy. Meanwhile, each of the Director

Defendants, in particular those that served on the Audit Committee, had knowledge of the "red flags" alerting them of Popular's overstatement of its deferred tax assets and earning because they reviewed all of the Company's financial statements. Had the Director Defendants caused the Company to promptly account for Popular U.S.'s deferred tax assets, the Company's reported earnings would have been significantly diminished, but the Company would not be exposed to liability now. Nonetheless, the Director Defendants exposed Popular to liability under the Securities Act of 1933 by causing the Company to conduct the Series B Offering in violation of their fiduciary duties to Popular. Moreover, each Director Defendant caused and/or permitted Popular to issue the false and misleading statements and financial reports detailed herein, exposing the Company to immense liability under the Securities Exchange Act of 1934 and to purchasers of its common stock between January 24, 2008 and February 19, 2009.

250. Accordingly, demanding that the Director Defendants take action before this lawsuit was filed would have been futile and, therefore, the demand requirement is excused.

AIDING AND ABETTING AND CONCERTED ACTION

251. In committing the wrongful acts alleged herein, each Individual Defendant has pursued or joined in the pursuit of a common course of conduct and acted in concert with one another in furtherance of their common plan. In addition to the wrongful conduct herein alleged as giving rise to primary liability, the Individual Defendants further aided and abetted and/or assisted each other in breaching their respective duties.

252. The purpose and effect of the Individual Defendants' common course of conduct was, among other things, to disguise their violations of law and breaches of fiduciary duty, and to enhance executive and directorial positions and receive substantial compensation and/or fees as a result thereof.

253. The Individual Defendants engaged in a conspiracy, common enterprise and/or common course of conduct during the relevant period. During this time, the Individual Defendants caused the Company to conceal the true fact that Popular was misrepresenting the financial status of its business and financial results.

254. The Individual Defendants accomplished their common enterprise and/or common course of conduct by causing the Company to purposefully, recklessly or negligently violate state and federal law, the federal securities laws, and abdicate their duties as directors. Each Individual Defendant was a direct, necessary and substantial participant in the common enterprise and/or common course of conduct complained of herein.

255. Each Individual Defendant aided and abetted and rendered substantial assistance in the wrongs complained of herein. In taking such actions, each Individual Defendant acted with knowledge of the primary wrongdoing, substantially assisted the accomplishment of that wrongdoing and was aware of his or her overall contribution to and furtherance of the wrongdoing.

256. At all times relevant hereto, each Individual Defendant was an agent of each of the other Individual Defendant and were at all times acting within the course and scope of such agency.

FIRST CAUSE OF ACTION
For Breaches of Their Fiduciary Duties of Loyalty and Good Faith
(Against All Individual Defendants)

257. Plaintiff incorporates by reference all prior paragraphs as if fully set forth herein.

258. The Individual Defendants each owed Popular and its shareholders the highest fiduciary duties of loyalty, good faith and due care in managing and administering the Company's affairs.

259. The Individual Defendants were required to exercise reasonable and prudent supervision over the management, practices, controls and financial affairs of Popular. By virtue of their duties of loyalty, good faith and due care:

(a) The Individual Defendants were required to exercise reasonable control and supervision over the Company's officers, employees, agents, business, and operations;

(b) The Individual Defendants were required to make inquiries, use sound business judgment, and remain informed about Popular's financial performance and operations, and upon receiving notice or information of an imprudent, unsound or unlawful decision, condition, or practice, the Individual Defendants were required to undertake a reasonable investigation in

connection therewith, were required to undertake steps to correct the decision, condition, or practice, and to make public disclosure of such decisions, condition, or practices in a timely and forthright manner; and

(c) The Individual Defendants were required to accurately calculate and report to Popular's shareholders the value of the Company's assets.

260. The Individual Defendants breached their fiduciary duties owed to Popular and its shareholders, or aided and abetted in the breach of other defendants' fiduciary duties, by willfully, recklessly and intentionally failing to perform their fiduciary duties. They caused the Company to waste valuable assets, unnecessarily expend corporate funds, and failed to properly oversee Popular's business, rendering them personally liable to the Company.

261. Each of the Individual Defendants had actual or constructive knowledge that they had caused the Company to improperly misrepresent the financial health of the Company and failed to correct those representations.

262. All Individual Defendants, singly and in concert, engaged in the aforesaid conduct in intentional breach and/or reckless disregard of their fiduciary duties to the Company.

263. The Individual Defendants conspired to abuse, and did abuse, the control vested in them by virtue of their high-level positions in the Company.

264. As a direct and proximate result of Individual Defendants' breaches of their fiduciary duties of loyalty, good faith and due care, and aiding and abetting those breaches, as alleged herein, Popular has sustained and continues to sustain significant damages and a drastic diminution in value. As a result of the misconduct alleged herein, the Individual Defendants are liable to the Company.

SECOND CAUSE OF ACTION
For Gross Mismanagement
(Against All Individual Defendants)

265. Plaintiff incorporates by reference all prior paragraphs as if fully set forth herein.

266. As detailed more fully herein, the Individual Defendants each owed a duty to Popular and its shareholders to prudently supervise, manage and control Popular's operations.

267. The Individual Defendants, by their actions or inactions, either directly or through aiding and abetting, abandoned and abdicated their responsibilities and duties to prudently manage Popular's business and assets.

268. As such, the Individual Defendant subjected Popular to the unreasonable risk of substantial losses by failing to exercise due care and by failing to use sound business judgment, including their failure to understand and monitor the Company's fiscal and financial performance. The Individual Defendants breached their duties of due care and diligence in managing and administering Popular's affairs and by failing to prevent a waste of Company assets.

269. When discharging their duties, the Individual Defendants knew or recklessly disregarded the wrongful conduct described herein, and either approved management's activities or failed to supervise such activities in accordance with their duties. The Individual Defendants grossly mismanaged or aided and abetted the gross mismanagement of Popular and its assets.

270. As a direct and proximate result of the Individual Defendants' breaches of their fiduciary obligations of loyalty, good faith, and due care, Popular has sustained damage and continues to sustain significant damages and a drastic diminution in value. As a result of the misconduct alleged herein, all Individual Defendant are liable to the Company.

THIRD CAUSE OF ACTION
Derivative Claim for Waste of Corporate Assets
(Against All Individual Defendants)

271. Plaintiff incorporates by reference all prior paragraphs as if fully set forth herein.

272. Because of the Individual Defendant's misconduct, Popular will incur costs and fees in the millions of dollars defending lawsuits and satisfying adverse judgments or settlements.

273. As a result of the conduct alleged herein, the Individual Defendants have unreasonably and unnecessarily caused Popular to waste valuable corporate assets.

274. As a direct and proximate result of the Individual Defendants' breaches of their fiduciary obligations of loyalty, good faith, and due care, Popular has sustained and continues to

waste precious corporate assets and thus sustain damage. As a result of the misconduct alleged herein, the Individual Defendants are liable to the Company.

FOURTH CAUSE OF ACTION
Derivative Claim for Unjust Enrichment
(Against Auditor Defendant, PwC)

275. Plaintiff incorporates by reference all prior paragraphs as if fully set forth herein.

276. By its acts and omission, PwC was unjustly enriched in the amount of approximately $16 million. To date, neither the Director Defendants nor the Company has made any effort to recoup, on the Company's behalf, the profits obtained by PwC's failure to properly audit the Company's financial statements in violation of GAAP and GAAS. PwC has been and will continue to be unjustly enriched at the expense of and to the detriment of the Company and it would be unconscionable to allow PwC to retain the benefits of its illegal conduct. The Company is entitled to recover these improperly obtained profits.

277. Plaintiff, as a shareholder and representative of Popular, seeks an order of this Court disgorging all profits, benefits and other compensation obtained by PwC from its wrongful conduct and fiduciary breaches and other relief for the Company, in an amount to be proven at trial.

PRAYER FOR RELIEF

278. WHEREFORE, Plaintiff prays for judgment in the Company's favor against the Individual Defendants as follows:

A. Determining this action is a proper derivative action, Plaintiff is an adequate representative on the Company's behalf, and demand is excused;

B. Determining the Individual Defendants have breached or aided and abetted the breach of their fiduciary duties to Popular;

C. Declaring that the Individual Defendants are obligated to indemnify and hold Popular harmless from any fines, penalties, judgment, settlement or award pursuant to any of the class actions pending or to be filed against Popular or its employees or agents arising out of the breaches of duty and wrongdoing alleged herein;

D. Awarding Popular the damages it sustained due to the violations alleged herein from each of the Individual Defendants jointly and severally, together with interest thereon;

E. Awarding Popular exemplary damages in an amount necessary to punish the Individual Defendants and to make an example of the Individual Defendants to the community according to proof at trial;

F. Awarding Popular restitution from each Defendant;

G. Ordering all Individual Defendants to return to Popular all incentive-based or equity-based compensation paid to them by the Company during the time they were in breach of their fiduciary duties that they owed to Popular;

H. Awarding Popular equitable or injunctive relief as permitted by law;

I. Awarding Popular punitive damages;

J. Directing Popular to take all necessary actions to reform and improve its corporate governance;

K. Awarding pre-judgment and post-judgment interest as allowed by law;

L. Awarding Plaintiff the costs and disbursements of this derivative action, including reasonable attorneys' fees, costs and expenses; and

M. Granting such other and further relief as the Court deems just and proper.

JURY DEMAND

Plaintiff demands a trial by jury on all issues.

DATED: November 20, 2009

LUIS E. MIÑANA & ASOC.
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Attorneys for Plaintiff

VERIFICATION

I, Luis E. Miñana, hereby declare as follows:

1. I am counsel for plaintiff in the above-entitled action. I have read the foregoing Complaint and know the contents thereof. I am informed and believe the matters therein are true and on that ground allege that the matters stated therein are true.

1. I make this Verification because plaintiff is absent from the County of Puerto Rico where I maintain my office.

Executed this 20th day of November, 2009, at San Juan, Puerto Rico.

Dated: November 20, 2009

/s/ Luis E. Miñana
LUIS E. MIÑANA